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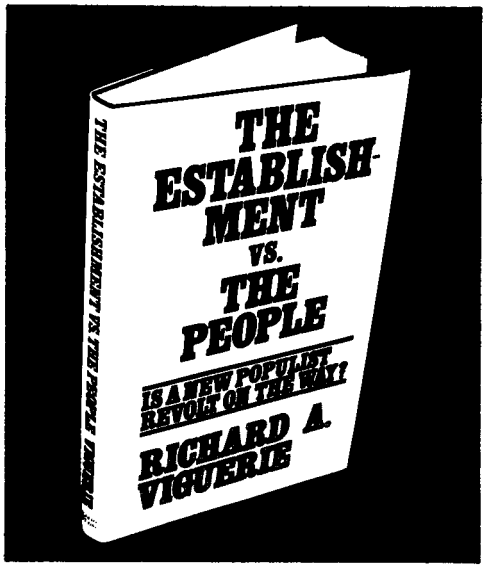

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—Patrick J. Buchanan,
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—Howard Phillips,
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The Conservative Caucus

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FIFTEENTH ANNIVERSARY YEAR

JANUARY 1984/VOL. 15, NO. 9

reason

Free Minds and Free Markets

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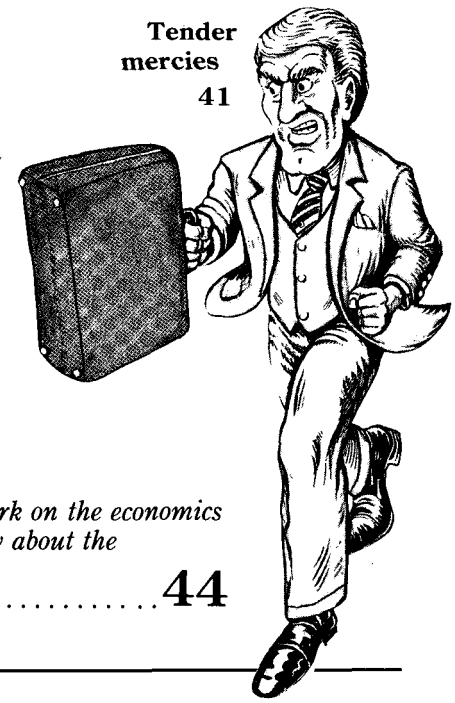

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NOTEs

I'm pleased to announce the promotion of Marty Zupan to editor-in-chief. My own responsibilities as president of the Reason Foundation have left me less and less time to devote specifically to REASON's editorial side. With Marty's full-time attention, REASON should do an even better job of keeping on top of current issues and emerging developments. One of her first actions as editor-in-chief was to reorganize the editorial department, putting Eric Martí in charge of production as managing editor.

REASON contributors continue their active participation in public-policy debates. David Henderson had an excellent article, "The Myth of MITI," in the August 8 issue of *Fortune*. Steve Hanke debated Gaylord Nelson, president of the Wilderness Society, on the policies of James Watt on Cable News Network, September 28. Fred Miller had an excellent article on the Third World infant formula controversy in *Barron's* on September 26, citing James Hickel's December 1981 article from REASON. And John Baden's new think tank, the Political Economy Research Center, received a full-page write-up in *Business Week*'s October 24 issue.

REASON contributor Don Feder, who is also editor of the newsletter *On Principle*, is now a *Boston Herald* columnist as well. That brings to three the number of Boston-based columnists with individualist/free-market perspectives, the other two being Warren Brookes (interviewed in REASON in the October issue) and REASON Contributing Editor David Brudnoy.

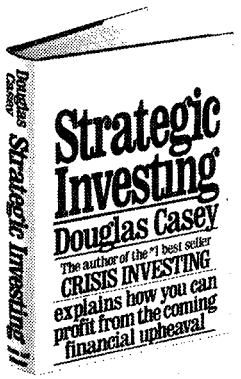
The Reason Foundation's people are a busy group, traveling and speaking on behalf of liberty in many contexts. In October, I traveled to Connecticut to present a paper on privatization of roads and bridges at the annual meeting of the Eno Foundation for Transportation. It will be published in a forthcoming issue of Eno's *Transportation Quarterly*. I also gave a talk based on the Reason Foundation's forthcoming book, *Defending a Free Society*, at the Future of Freedom Conference in Long Beach. Also over the fall, Senior Editor Manny Klausner and I took part in a Los Angeles seminar on monetary reform, organized by Reason Foundation trustee Joe Coberly for the Committee on Monetary Research and Education. Manny also took part in a Denver conference on private education and the law, sponsored by Mountain States Legal Foundation. And he and I have both joined the advisory board of the new National Council for Better Education; a market-oriented group, whose chairman is frequent REASON contributor Sam Blumenfeld.

On the publication front, Senior Editor Tibor Machan and former trustee M. Bruce Johnson have coedited the book *Rights and Regulations*, just released by the Pacific Institute. Assistant Editor Paul Gordon continues to be featured frequently on the op-ed page of *USA Today*, most recently (October 25) on education vouchers. My own piece on airline deregulation appeared on that page October 4. And I was pleased to be one of a group of distinguished contributors (including Martin Anderson, Robert Bartley, George Gilder, Arthur Laffer, and Jude Wanniski) to an *American Spectator* symposium on the subject, "Is Supply-Side Economics Dead?" appearing in the magazine's November issue.

Several more REASON articles have been reprinted, thereby reaching much wider audiences. Patty Newman's hard-hitting "Harvest of Power" (September) was reprinted in the *Arizona Republic*'s Sunday feature section on September 18. The Reading Reform Foundation has become the latest in a long list of educational groups to reprint Sam Blumenfeld's "The Victims of 'Dick and Jane' " (from October 1982). And *Locus*, the leading science fiction fan magazine, is reprinting Poul Anderson's review of Neil Schulman's book *The Rainbow Cadenza* from our October issue.

Here's an organization you should know about if you're thinking of teaching your kids at home but fear possible legal hassles. The Home School Legal Defense Association (Box 26280, Fort Worth, TX 76121) offers an insurance-like service for home schoolers. For an annual $65 membership fee, they say they will provide complete legal representation in the event of threatened or actual legal action. Their brochure includes an endorsement from Dr. Raymond S. Moore, an authority on home schooling whose work was discussed in our April cover story on the subject.

—R. W. P.



Forbes reports: This man's investment portfolio is up 54.5%

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★ Five reasons why you should take another look at utilities — *but only these certain few.*
★ Why the strategic metals boomlet will ensnare many an investor — and yet may be worth a flyer. How to buy. Where to buy.
★ A relatively safe way to speculate in commodities — and you don't have to be an expert or sit watching a computer. The three rules that help you profit (and keep your peace of mind). How to buy far-out contracts *without* paying the premium. (Doug monitors some 15 commodities regularly for his readers, and also recommends several brokers who have given him good service.)
★ Stocks to short — individual issues as well as vulnerable industry groups. Six clues to picking a good short. Why you should weigh *all six*. How to, in effect, short the market as a whole.
★ Why almost everyone should stay out of rare coins, stamps, art, etc.
★ What a depression really is. The three major causes. (The first covers acts of God — which we can't control. The other two? We're already suffering from both!) Three ways the Great Depression of the 30s differs from the Greater Depression of the 80s. How to cope.
★ Biotechnology stocks — and why Doug told his readers to dump them when they were riding high.
★ South African golds: charted, graded and marked for buy/sell/hold. Major North American golds, junior Canadian golds, junior American golds — all analyzed for buy/sell/hold.
★ The one auto stock — yes, auto stock! — you should watch. Why it looks like one of the great overlooked bargains of the 80s.
★ You don't know how to play the Singapore market? It's not hard. Why it almost always pays to keep part of your investments abroad. How to sniff out the coming bull markets in other countries (all of which Doug monitors for you). One stable, friendly, prosperous country where nearly all the growth lies ahead.
★ How to distribute your money among the various *types* of investment. (Revised regularly to keep you protected against all developments.)

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EDITORIAL

Robert W. Poole, Jr.

Don't Hang Up on Competition

Decade after decade, populist politicians and consumer advocates attacked Ma Bell, railing against the evils of the phone monopoly. Today, their victory is nearly complete, thanks to a decade of deregulatory moves by the Federal Communications Commission (FCC) and a seven-year Justice Department antitrust case. But just as the hated monopoly is finally expiring, a rump protest in Congress threatens to undo much that the deregulators have wrought. Ironically, the protestors are. . . the populists and consumer advocates!

What's happened is a failure to think through what competition—the only alternative to monopoly—really means. For most of this century, plain old telephone service was all there was, and it was provided by monopoly firms, most of them part of the Bell System (AT&T). To promote "universal service," both the regulators and the companies supported a whole system of subsidies. Long-distance users were systematically overcharged to subsidize local customers; and long-distance rates were averaged, so that high-traffic routes subsidized low-traffic ones.

That, of course, is *one* way to run a telephone system. But it's a costly one, both in the arrogance of a monopoly provider and in the inefficiency bred by subsidies and lack of competition. As new technologies came along in the 1960s, competitors began chipping away at the monopoly's edges. First the FCC legalized "foreign attachments"—non-Bell phones, answering machines, PBXs, etc. Later it began allowing firms like the pioneering MCI to offer discount long-distance services. By the late '70s, the monopoly was in shreds.

Consumers have benefited enormously from these changes. Today you can purchase your own cordless, memory-dialing, privacy-screening telephone from any of dozens of firms, saving a fortune over leasing (forever) from Ma Bell. And you can choose from a variety of long-distance companies, at rates as much as 50 percent lower than Bell's. Lower rates and all-digital links have enabled businesses to take full advantage of the computer revolution, transmitting huge volumes of data, often as a substitute for costly travel.

The breakup of AT&T is simply the culmination of these trends. With long-distance service increasingly digital and competitive, it made no sense for Bell to be stuck forever with artificially high long-distance rates to subsidize local users. So as part of the breakup that is spinning off local Bell companies, the FCC wants to allow the new (long-distance) AT&T to price competitively. To make up for the loss of subsidy at the local level, the FCC would allow the locals to charge an additional flat monthly fee—called an "access charge"—on the grounds that customers should pay for the local line that gives them access to the long-distance network.

It is this "access charge," and the resulting increase in the local portion of phone bills, that has aroused the populists in Congress. Yet once the FCC allowed companies like MCI to begin competing in long-distance eight years ago, it was *inevitable* that long-distance charges would no longer be able to subsidize local service—and therefore that local rates would have to go up. Yet it is only now, when the horse has long since galloped out of the barn, that the politicos are trying to slam the door.

The would-be reregulators realize what a bind their inattention has put them in. They cannot simply forbid the local access charges and require that AT&T continue to subsidize the local companies. That would drive more long-distance users to the new competitors. So they want to tax *all* long-distance users, on a per-minute basis, to raise funds for local subsidies. But that will only prompt more large business users to build their own private systems to bypass the common carriers altogether. So the pols want to tax bypass systems, too. In other words, if you develop, at your own expense, a microwave/satellite cross-country telecommunications system, you will still have to pay a tax so that Joe Smith can get cheap phone service at his weekend cabin in the Rockies. And this is being advocated in the name of fairness!

What lies behind such measures is the wrong-headed idea that telephone service is a right and some people must be forced to provide it for others. The opposite idea is that telephone service, like other goods, is a matter of choice—and that those who choose to live in low-demand, high-cost areas should be free to make that choice *and pay the price.* This is the principle we've accepted in deregulating airlines, trucks, and buses. It's working well, providing large cost savings and more choices of service for most users and only modest cost increases or reductions in service for small numbers of users. The same will be true for telecommunications.

We are just at the beginning of a revolution in telecommunications spawned by advancing technology. As Peter Samuel pointed out in REASON in October, the advent of cellular radio networks, microwave links, fiber-optic circuits, two-way cable, "intelligent" phones, and home computer terminals opens the door to a host of services whose exact forms we can only imagine. Which of these will be provided by local cable companies? Which by local phone companies? Which by radio common carriers? *Nobody knows.*

But those who would reassert regulatory control are making one huge assumption: that regulators know better than competing firms and consumers who should develop which technology and how each should be marketed and priced. Whether inspired by panic over losing control or by sheer political opportunism, the regulatory impulse is wrong and must be resisted.

It is wrong because it seeks to undo a decade of progress toward user-pays telecommunications. It is wrong because it risks holding back an explosion of new and beneficial services. But most of all it is wrong because it would substitute *force* for *choice.* Deregulating telecommunications is not merely sensible; it's also the right thing to do.

Robert W. Poole, Jr.

THE AUSTRIAN ECONOMICS PROGRAM

AT GEORGE MASON UNIVERSITY

The study of economics at George Mason University continues to expand and diversify. The Economics Department now offers degrees at both the master's and doctoral levels; the prestigious Center for the Study of Public Choice joined the department in June, 1983; and the Center for the Study of Market Processes and its Austrian Economics Program continue to grow.

Students and faculty meet at Austrian economics colloquium.

FACULTY. George Mason now has four full-time faculty members familiar with Austrian Economics: Karen Vaughn, Ph.D., Duke University; Don Lavoie, Ph.D., New York University; Jack High, Ph.D., UCLA; and Richard Fink, Director of the Center for the Study of Market Processes, who is presently completing his degree at New York University. Another faculty member this year is visiting scholar John Egger, who is completing his degree at New York University.

Besides teaching graduate and undergraduate courses, the faculty members direct research and conduct seminars on subjects of interest to Austrian economics students.

CENTER FOR THE STUDY OF MARKET PROCESSES. The Center, which directs the Austrian Economics Program, was established to encourage the study of the market as a dynamic process. Among its many activities to promote Austrian education and research are: guest lectures and conferences on topics related to the market process; a weekly Austrian economics colloquium to allow students and professors to interact on a more informal basis; a scholarly newsletter, *Market Process*; and a writing program for Austrian students. Now in its third year, the Center has drawn considerable support from businesses and foundations.

Ph.D. PROGRAM IN ECONOMICS. The program requires students to successfully complete a number of courses in economic theory and quantitative methods, to demonstrate a competence in at least two fields of specialized study, and to produce a substantial body of original research.

Of particular interest to Austrian students is a year-long course in Austrian theory and policy. This course includes the study of methodology, Austrian utility theory, competition and entrepreneurship, monetary theory, socialist calculation, and business cycle theory. This year-long course makes George Mason one of the few institutions to offer in-depth training in the Austrian tradition.

A limited number of graduate fellowships and research assistantships are awarded on a competitive basis.

For further information or an application for admission, contact *Sharon Gable, Center for the Study of Market Processes, George Mason University, 4400 University Drive, Fairfax, Virginia 22030, (703) 323-3483.*

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Letters

Dismantle for Disarmament?

Jack Wheeler ("How to Dismantle the Soviet Empire," Nov.) writes well, his heart is in the right place, and REASON was right to publish his provocative article. However, he makes some of the same errors as the CIA.

The "nationalities" problem, whose treatment by Stalin first brought him to Lenin's attention, has been recognized as one of the breeders of discontent and revolt in the USSR by many writers, including me in *Power Through Subversion* (1972). As the history of subversion therein related shows, revolt and overthrow must come from within, although in the USSR, they can and should be nourished even in the preparatory stage by money and, when propitious, by arms from without.

Mr. Wheeler has fallen into the treaty trap; the aim of reaching a disarmament pact with the USSR is erroneous. All nations have regularly broken their treaties, and disarmament treaties cannot be "verified" by "national technical means." Moreover, it will hardly inspire the trust of dissidents to inform them that we intend to help them in order to obtain disarmament and, if achieved, to abandon them. Their reason for dissidence is not armament but rather the conditions imposed on them by their Moscow masters.

Laurence W. Beilenson
Los Angeles, CA

Alienated Aged?

Someone tell Mr. Davidson to settle down ("Weep Not for the Wizened," Viewpoint, Oct.). Someone tell him that every elderly person that he blames for the mess this country is in is a potential supporter of liberty. Sure, they voted for the clowns that have brought this country to its economic and moral knees. That's what they were taught to do. Vote, don't think. Obey, don't question.

Davidson gives a decisive and unarguable position on Social Security. Why not leave it at that? Instead, he continues on and hammers away at the unsuspecting and innocent elderly reader, placing entire blame for the mess this country is in on their shoulders. In my opinion, if Davidson's purpose was to alienate the elderly from an individualist view of Social Security, he succeeded.

Robert D. Johnson
Midland, MI

Burned Up

Please cancel my subscription immediately. The article by Mr. Davidson in your October issue was such an anti-elderly collection of slop as I have ever seen in my life. I can't think of anything that burns me up more than someone who is so arrogant, sneering, and pompous and thinks they have all the answers to the problems of the world like you people do. Well, someday your philosophy is going to blow up in your face.

Guy W. Loeb
San Diego, CA

Whose Counting?

Just for the record, did Tibor Machan ("You Can't Have Marx Without Stalin," Oct.) *really* mean to write that "an estimated 250 million people have been murdered in the Soviet Union alone"—or was this a typographical error that went uncorrected? And, if he really *did* mean to write that, who is responsible for this grossly inflated "estimate" of the number of victims of Soviet Communism?

L. A. Rollins
Los Angeles, CA

Puzzling Quandary

Tibor R. Machan's quandary about the intellectual appeal of communism seems contrived. Among other things:

There is nothing wrong with man building "on past visions while urging more modern methods." Intellectual man *does* envision a society where the monarchs, oligarchs, and robber-baron capitalists are not the only ones who can be individualists and exercise the right of property. Such a society is barely more than a vision; and, incorrect though it is, communism is, for the visionary, the most cogent social doctrine of our time. Unfortunately, anticommunists have little to offer except rhetoric such as Machan's. Good rhetoric though it may be, it has little intellectual appeal.

Though the appeal of communism for some men may be the altruistic pretensions of Marx, most men are attracted to communism precisely because it is an intellectual basis for egoism and authoritarianism. But certainly altruism is not bad because a pretended altruist developed an egoistic doctrine. Moreover, altruism is not necessarily a "moral imperative of individual self sacrifice." Altruism can be no more than the granting to others of the right to live their lives in peace. And it is altruism, not egoism, which is compatible with individual liberty in the political realm....

The most important intellectual appeal of communism is one which Machan either ignores or is ignorant of—dialectics. Dialectics is a profound intellectual, philosophical concept which is a fundamental part of communist thinking. Those who would oppose communism on a logical instead of a rhetorical basis need come to grips with that concept.

Bernard Curry
Glendale, CA

Mr. Machan replies: The estimate of 250 million was made by Robert Conquest, noted Sovietologist. It is interesting that Mr. Rollins knows that this is a "grossly inflated 'estimate' of the number of victims of Soviet Communism" prior to checking out the basis of it. I found it incredible myself, but I examined the method of estimation, and my mind was changed.

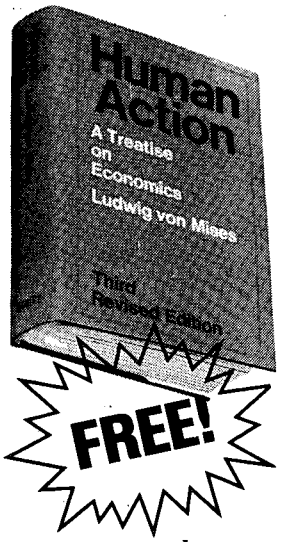
Regarding Mr. Curry's letter: Visions, like "the brotherhood of humankind," are bad in any case but mainly because they are nothing but empty fantasies—visions. The rest of Mr. Curry's letter I am unable to follow.

Why Stalin

The relationship between Marx and Stalin can be easily explained using the analysis provided by Robert Nozick in *Anarchy, State, and Utopia.* A theory of justice holds either that certain *processes* are just or unjust or that certain *results*

(Continued on p. 63)

Communicate with REASON. Box 40105, Santa Barbara, CA 93103. We appreciate receiving your letters typed double-space and limited to 200 words. Letters sent to REASON will be considered for publication (unless otherwise noted) and may be subject to abridgement or editorial comment.



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brickbats

Alice Drefchinski has been penalized $500 by the feds for exercising her right of free speech. The Louisiana registered nurse was accused of filing a "frivolous income tax return" because she let the IRS know about her religious convictions against war. Her crime was to include a letter with her tax return to protest defense spending and ask that part of her taxes, which she called a "war tax deduction," go to a humanitarian organization. Miss Drefchinski hadn't failed to ante up any of what the IRS says she owed. In fact, the government owes *her* $719 in overpayments. An IRS spokesman defended the penalty because protest letters attached to tax returns make them difficult to process. "There is no such thing in the tax code as a war tax deduction," he says. "The government doesn't recognize a philosophical or moral argument."

From the Why Can't Johnny Read Dept.: A janitor taught two social-studies classes in a Detroit high school, and nobody was the wiser until he confessed to the deed. Andrew Ranson, on a temporary janitorial assignment, reported to the main office at Redford High School instead of to the head custodian. When he told the edu-crats he was a substitute, they gave him a lesson plan and sent him forth to educate—which he did. Either teaching doesn't really require all those fancy education courses, or teaching standards have slipped so low that nobody could tell the difference.

It's a dog's life all over, but nowhere worse than in Peking. The Chinese have denounced "running dogs" for years, and now they've done something about it. They've banned all pet dogs from the capital city, with two exceptions: guide dogs and dogs bred for the wok. Even the strictest revolutionary won't outlaw such a delicacy.

Edward J. Brown was pulled over a few years ago by a New Jersey state trooper because of a loose license plate on the Corvette he had lovingly restored from spare parts. The car, the cop noticed, had a 1966 body but a 1964 registration. Then he found different serial numbers on various parts. The trooper was convinced that Brown had received stolen property. After Brown explained to a judge that he was just a Corvette buff, the charges were dropped. But that wasn't the end of Ed Brown's troubles.

State officials refused to release his car, citing a statute that allows a car to be seized when it's operated under "suspicious circumstances." A state appeals court finally ordered the car returned, chiding the officials for ignoring the sworn testimony of the auto wrecker who had sold Brown most of the parts. Happy ending? Nope. When Brown went to the towing shop where the car had been impounded these past six years, his beloved Corvette was nowhere to be found. Seems there was a dispute between the tow shop and state police about storage fees, so the tow shop sold the sports car.

THE E.P.A. TODAY REPORTED A NEW THREAT TO THE CLIMATE, CALLED THE "WHITEHOUSE EFFECT",
WHICH IS PRODUCING OVERHEATED AIR MASSES, MELTING PRINCIPLES, AND RAPIDLY RISING BILGEWATER LEVELS.
THIS IS APPARENTLY CAUSED BY THE UNCONTROLLED YEARNING OF FOSSIL FOOLS FOR HIGHER OFFICE....

Why on earth did the US Navy buy 57,600 softballs? The House Defense Appropriations Subcommittee said the softball purchase was only part of a gigantic spending spree made last September 30 by all military services to rid their coffers of appropriations for the 1982-83 fiscal year. So the answer is simple. The Navy spent the money because it was there.

New York Mayor Ed Koch is many things, but subtle he ain't. Hizzoner is 100 percent in favor of the United Nations remaining in his city. Why? "Because every country needs a cesspool. And the UN is always interesting as a theater of the absurd."

Rosemary Furman of Jacksonville, Florida, runs a legal-forms business and, for nominal fees, helps poor people fill out routine court papers. "Every time I make $50, some lawyer loses $500 or $5,000," she says. Which probably helps explain why the Florida Bar Association got a court order against her for practicing law without a license. "I was accused by lawyers, tried by lawyers, and will be sentenced by lawyers," she says, adding that her only real crime is exposing lawyers who practice without a conscience.

When you need to send a message fast, do you rely on the US Postal Service or on a private delivery company? The answer is obvious—even to the federal government. Sometimes the feds need to tell that nationalized enterprise called the Postal Service not to deliver a retirement check to a recipient who's been found ineligible. In this case, haste saves waste, and so local post offices are advised via a Western Union mailgram to send the errant checks back to the Treasury. Why not use the Postal Service to send a message to the post office? Why send a tortoise on a hare's mission?

—MARK EDWARD CRANE

HOW YOU CAN PROFIT BY LEARNING POLITICIANS' DIRTY LITTLE SECRETS

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TRENDS

MILKING THE CONSUMER

Free-market advocates have long known that consumers pay through the nose for milk and milk products because of the federal government's dairy price supports. Lately, however, free marketeers have been joined by some unlikely allies in opposition to subsidizing dairy farmers.

In October, that pillar of the liberal establishment the *New York Times* published an editorial lambasting dairy price supports. "They are costing the taxpayers close to $3 billion a year, and Government warehouses are bulging with billions of pounds of surplus cheese, butter and powdered milk," the paper fumed.

The *Times* rarely supports measures as radical as immediately doing away with a bad program. In this case, the paper was in favor of a proposal to reduce the price support level gradually from $13.10 per hundred pounds to $11.60. "All dairy farmers would lose some money and some would be forced out of business," conceded the editorial. "But that has to happen if the Government is ever to get rid of these subsidies. As a group, dairy farmers are not more deserving of welfare payments than, say, architects or hardware store owners."

The same month as the *Times* editorial, the *Atlantic* published a detailed account of the dairy boondoggle, "The Political Economy of Milk," written by John Donahue, a doctoral fellow at Harvard University's John F. Kennedy School of Government. Donahue pointed out that the price-support program costs $2.4 billion this fiscal year alone—which averages out to about $10,000 for every dairy farmer in America—plus an estimated "couple of billion dollars a year" in higher supermarket prices.

A standard defense of price supports is that they provide consumers with stable prices. The trouble is, noted Donahue, that "farmers like prices stable and high while consumers like them stable and low. The present system resolves the issue by making consumers pay high prices all of the time in order to spare them from paying high prices some of the time."

Donahue might also have mentioned the absurdly large amounts of dairy products stored by the government solely to prop up dairy prices. REASON pointed out in "How to Get Out of the Food Stamp Trap" (Aug.) that the feds were hoarding *11.4 billion pounds* of nonfat dry milk in early 1983 and 1.5 billion pounds of other dairy products.

Still, Donahue did conclude that dairy price-support policies are extremely inefficient ("marketing orders are pure Rube Goldberg economics"). They "shackle American efforts to liberalize world trade in farm goods." And they redistribute wealth "to benefit farmers who are able-bodied, competent, and often a good deal wealthier than the average American."

Meanwhile, three liberal citizens' organizations—a Hispanic veterans group called the American GI Forum, the Gray Panthers, and the League of Latin American Citizens—have also voiced strong opposition to the dairy boondoggle. Their representative, a San Francisco public-interest lawyer named Robert Gnaizda, testified before the President's Task Force on Food Assistance that American cheese sells for about twice the world market price because of the subsidies. He also noted that ending dairy price supports would reduce cheese prices to 83 cents per pound.

Gnaizda condemned agricultural subsidies as "America's largest welfare system." As for dairy price supports, "Ending the subsidy will finally make cheese affordable to the poor," he said to the task force. "This is the way to solve hunger consistent with free-market principles and dignity for all."

WORLD DEBT AND THE MONETARY ORDER

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Joseph Gughemetti, attorney for Bruno and Eugenia Martino, told REASON that the case began in 1975 when the Martinos applied to local authorities in Morgan Hill, California, to subdivide their commercial property there and lease one acre to a fast-food restaurant. They were told that the local water district required them to dedicate 21,000 square feet of land to the district for free and to reserve another 36,000 square feet that the district required for a planned flood-control project and would condemn and pay for under eminent domain.

The Martinos waited for the condemnation proceedings on the 36,000 square feet so that they could proceed with development—and waited some more. Then in 1980, when they asked the water district when the property would be condemned, they were informed that 108,000 square feet—two-thirds of the acre that the Martinos wanted to lease out, plus some adjacent property—had been slated for public acquisition since 1968. Moreover, they were told that they would have to wait at least *six more years* for the condemnation proceedings, and if they tried to develop their property before that time, they would have to dedicate the 108,000 square feet to the water district for free.

At this point, the Martinos had had enough. Their attorney brought a suit arguing that the city government and the water district had violated the Martinos' property rights under the 1964 Civil Rights Act and asking for compensation.

The Martinos were issuing a head-on challenge to a precedent set in 1979 in *Agins* v. *City of Tiburon.* In *Agins*, the California Supreme Court had held that landowners are not necessarily entitled to compensation from government agencies for the "de facto taking" of their property. The *Agins* decision said that the most a property owner can hope for—even after years of litigation against an agency—is a formal hearing conducted by the very agency that took the property in the first place.

In the Martinos' case, a US district court held that the *Agins* precedent applied, precluding compensation for the Martinos. But last May, the Ninth Circuit Court of Appeals said that *Agins* is not a binding opinion and that citizens do have a right to recover damages from government entities for "unreasonable land use regulations." The Martinos' case was remanded to the district court for trial.

The attorneys for the city and water district applied to the Supreme Court to reconsider the case, but in October the Court refused. So the case will go to trial in a lower court this June—but this time around, the Martinos' property rights under the law will be far stronger than when their troubles started nine years ago.

Of course the case is significant for the Martinos personally. But it also establishes a precedent in the nine western states of the Ninth Circuit. In California alone, the difference could well be enormous, since property owners will be far less vulnerable to the depredations of ambitious planning agencies like the Coastal Commission, which have, via land-use regulation, been able in effect to confiscate property almost with impunity. If land-planning bureaucrats have to put money on the line, this could provide an effective restraint on their grand designs for other people's property.

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GETTING THE MESSAGE STRAIGHT

It would take the US Postal Service to botch the operation of one of the most promising telecommunications services—the delivery of messages via computer. And botch it it did.

When the USPS started up E-COM—for electronic computer-originated message delivery—in January 1982, the Postal Service predicted that the $40-million E-COM system would handle 45 million messages by the end of September 1983. In fact, by that date, E-COM had delivered less than 18 million messages in all. And that at a loss of $16.7 million in fiscal 1982 alone.

To use E-COM, a sender transmits his message via computer to a terminal located in one of 25 specially equipped US post offices. There, the message is printed out, stuffed in an envelope, and hand-delivered by a USPS mail carrier. Although the system sounds good, there are a number of drawbacks that account for its poor performance.

For one, the service's availability is limited, and its two-day delivery time is not a particularly compelling reason for businesses to use E-COM. Also, a minimum of 200 messages is required each time the service is used, and there is a two-page limit on each message sent. Moreover, reply envelopes cannot be used with E-COM, although these are essential for the billing or mail-order applications for which electronic mail is particularly well suited.

E-COM's critics—which include the Justice Department, the Federal Trade Commission, various members of the Postal Rate Commission and of the USPS board of governors, and the private telecommunications industry—have repeatedly warned against USPS involvement in electronic communications, fearing that the Postal Service could underprice electronic services by subsidizing them through revenues from its monopoly on the delivery of first-class letters. And indeed, the House Republican Research Committee in July reported that, thus far, "the actual cost of handling an E-COM message is $5.51," while the USPS charges only 31 cents for a two-page message.

But even cross-subsidies might not save E-COM from competition from private electronic-delivery services, to which MCI Communications Corp. added a new contender in September with its MCI Mail. Taking on E-COM—as well as other similar services from Western Union, GTE Corp., and Tymshare, Inc.—MCI Mail offers four different types of services, ranging from computer-to-computer message relay to laser-printed letters delivered to the final destination by courier just four hours after the letter has been transmitted.

Basing their predictions on MCI's past success and on the fact that the company has an extensive communications network—including a computer center near Chicago that can interconnect a variety of otherwise incompatible equipment—industry analysts see a bright future for MCI in the document-delivery field. And with that market estimated at $8 billion a year, other new competitors cannot be far off. It just goes to show you what a little dose of entrepreneurship will do.

MEANINGLESS MEASURES

Industrial-policy advocates—Harvard's Robert Reich, for example, or New York investment-banker Felix Rohatyn—like to believe that government planners

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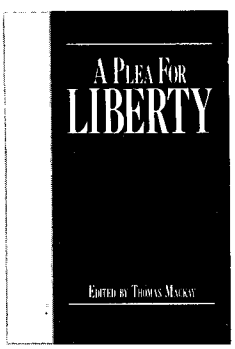

A Plea For Liberty
An Argument Against Socialism and Socialistic Legislation

Edited by Thomas Mackay
Introduction by Herbert Spencer
Foreword by Jeffrey Paul

Twelve essays, first published in 1891, by British authors investigating the impact of "social legislation" upon the people and economy of Great Britain and Australia at the turn of the century. The discussion is both theoretical and empirical. Among subjects considered are: labor unions and labor under coercion or freedom; the condition of the working class; effects of protectionism on labor, agriculture and industry in Australia; free libraries; the role of the State in education; the Post Office, State housing, and State ownership or regulation of utilities. Hardcover $13.50, Softcover $6.00.

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would have the wisdom to steer the nation's economy toward prosperity for all. Primary among their roadmaps are the various data collectively known as "economic indicators"—things like the Consumer Price Index, Gross National Product, and the many other aggregate statistics generated by both government bureaucracies and private research companies.

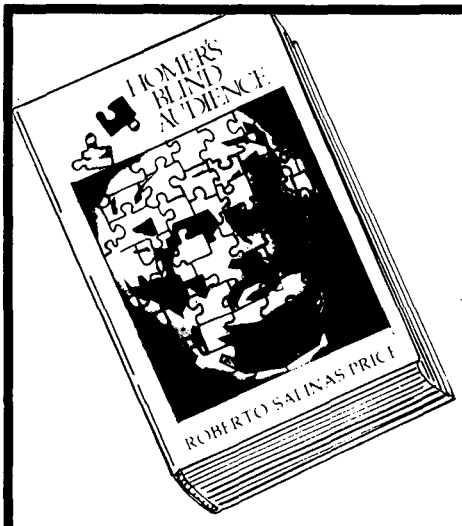
Critics of central planning—especially Austrian School economists like the late Ludwig von Mises and Friedrich Hayek—have long argued that these econometric measures and analyses cannot accurately represent a large, dynamic economy. And of late, skepticism about these efforts to amass statistics and create models of the economy based upon them has been growing.

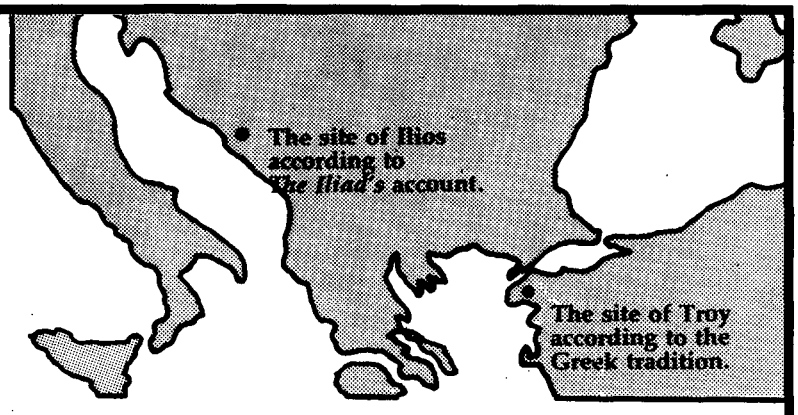
In a recent article discussing the failure of economic indicators to reflect the economy accurately, *Business Week* cited "the rapid structural change in the economy" as a major reason. Not only is the fast-changing economy outpacing statisticians' efforts to compile the relevant data, but the categories of data themselves are outdated. "Decisions about what constitutes a major industry," the magazine observed, "were made in the 1930s." Thus, for example, the government's Standard Industrial Classification Manual has no separate category for microprocessors, while the tobacco and leather industries—which, combined, account for less than one-half of one percent of total US output—are each listed as major industrial groups by government data collectors.

The use of outmoded categories and concepts explains why the government regularly understates economic measures such as the real value of GNP (by as much as 5 percent), industrial-capacity utilization, and productivity growth. And while updating the classifications to reflect the current weight of the various economic components would seem the obvious solution, there are several problems with that. It takes time to revamp the indicators, during which the economy may have changed so much that the "new" indicators would have become obsolete. But in addition, statisticians would no longer be able to compare data from time period to time period even if the categories could be adjusted often enough to keep up with the pace of economic change.

These inherent flaws may well explain the findings of a recent report issued by the Washington-based Cato Institute, in which analyst Randolph Boehm examined presidential economic and budget forecasts over a recent 10-year period to determine their accuracy. Boehm's study dramatically illustrates the failure of such forecasts. The average error of predictions of the next-year federal deficit, for example, was 529 percent. Forecasts of change in federal receipts from one year to the next were off by an average 87 percent, and those for change in GNP by 24 percent. The average error of forecasts of changes in the next year's Consumer Price Index has been 63 percent.

Indeed, so unreliable are these aggregate statistics that noted econometrician Wassily Leontief, long-time advocate of government planning, has acknowledged their inability to provide sound predictions. Quoted in an October 1983 *Los Angeles Times* op-ed piece by





An essay on *The Iliad's* geographical prerequisites for the site of Ilios.

The author contests the traditional location of King Priam's Troy in Asia Minor where Heinrich Schliemann discovered ruins that answer to the citadel of Ilios. The real Troy, he says, is located in what is now modern Yugoslavia and he offers literary and archaelogical evidence to that fact, arguing that Homer's Troy was transferred to Asia Minor by the Greeks for political reasons.

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Times science-writer Lee Dembart, Leontief noted that "the average econometric models give 50-50 accuracy, meaning as much accuracy as you can get if you toss a quarter." Leontief said that when natural scientists are asked why they don't use the econometricians' "fancy statistical methodology," their response is that if they " 'had to use those tools, we would chuck the whole business and get more facts.' "

THE SUBSIDY VS. SELF-SUPPORT SHOW

The final results of a 15-month test, concluded in June, in which nine Public Broadcasting Service TV stations aired paid commercials, show the experiment to have been a success. Advertisers, it appears, are eager to reach PBS's upscale audience: the nine stations earned a total of $4 million from the ads. And to the surprise of many, contributions from viewers actually *increased* during the experiment.

For the nation's 300 PBS stations, which face a 1984 budget of $130 million—down from $137 million in 1983—commercial advertising represents an attractive revenue source. Congress is expected to pass legislation next year on public-broadcasting funding. But if the legislators follow the recommendation of the Temporary Commission on Alternative Financing for Public Telecommunications, which oversaw the advertising experiment, PBS stations' path to that revenue source could be cut off.

The commission, composed of 11 individuals from government and PBS, recommended in September that PBS stations not be allowed to air traditional hard-sell commercials but only "expanded" messages by corporate underwriters of PBS shows. Its rationale: the stations might not be able to handle the new costs associated with going commercial (unions might up their wage and benefit demands, for example, and owners of properties aired on PBS might increase their copyright fees).

But several of the stations that participated in the experiment have attacked the commission's recommendation to prohibit commercials. One station's general manager, quoted in the *Los Angeles Times*, called it "absolutely ridiculous," noting that there had not been "a single bit of negative data from the experience." And another station executive, also quoted in the *Times*, said that other stations' choice not to air commercials "should not preclude those of us who wish to from testing this in the marketplace."

AIR SAFETY RIDDLE

Regulation by the Federal Aviation Administration has virtually no effect on aviation safety, concludes a recent Ph.D. dissertation by Andrew John Chalk. Yet flying is the safest mode of transportation. What accounts for this seeming paradox?

To begin with, the Washington University graduate student demonstrated the FAA's apparent irrelevance to safety. First of all, the agency's efforts to improve safety are not based on analyses of which projects might produce the greatest increase in safety for a given level of spending. Rather, Chalk shows that its priorities are determined by pressures from Congress and various interest groups.

Second, the FAA's level of enforcement of its regulations is "miniscule." For the entire airline industry, the total amount of fines assessed by the FAA is only about $100,000 a year. The average offense leads to a fine of just $1,000—hardly adequate to deter misconduct by firms grossing billions a year. Furthermore, most airlines significantly *exceed* safety regulations in areas over which they have discretion.

Chalk figured that something *other* than FAA regulation of airlines must account for aviation's high level of safety. He decided to test the hypothesis that aircraft manufacturers have a high stake in protecting their reputations by producing safe aircraft—accidents that damage reputation would decrease the value of the company's stock.

So Chalk examined a sample of 72 crashes between 1966 and 1979. In 23 of them, there were indications at the outset that the involved planes' designs may have been at fault; the other 49 crashes were used as a control group. Examining the post-crash behavior of the aircraft manufacturers' stock prices, Chalk found no effect for the control group, but a very significant drop in value following those crashes in which the design might have been at fault. In

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those cases, the *average* loss in shareholder wealth was $57 millon per crash. In the case of the 1979 Chicago DC-10 crash, McDonnell Douglas stockholders lost around $200 million.

Thus, Chalk concludes, reputation plays the major role in promoting safety, while the FAA continues to go through the motions of making rules and assessing token penalties.

WORKING BEHIND (PRIVATE) BARS

Nationwide, about 300 prison inmates—of a total of more than 400,000—are employees of private businesses, performing work ranging from operating telephone switchboards to manufacturing computer components. Private employers' contracting with inmates as workers had been illegal from the 1920s until 1979, when Congress passed a bill allowing seven experimental inmate-labor projects.

In one of the projects, the Minneapolis-based Control Data Corp. has hired 42 Minnesota inmates to assemble computer disk drives. In another project, 30 women prisoners in Phoenix are working

GLOBAL TRENDS

TWISTS AND TURNS ALONG BRITAIN'S PRIVATE ROUTE

GREAT BRITAIN—One of the most important positive developments in Great Britain is a genuine debate about the welfare state. Even the BBC used its flagship current-affairs program, *Panorama*, to analyze the future of government spending and taxation given present statutory commitments to entitlements, as they are called in the United States.

In one sense, the Tories are being very brave in attacking the sanctity of the welfare state. They have, for example, actually lopped off administrators from the National Health Service. In another sense, the party's commitments are a load of talk and not much go. Lord Carrington, the former foreign minister, came out and suggested that perhaps it is time for government to reduce its welfare functions. The thought was absorbed, sagely accepted as perhaps an inevitability, and nothing has happened since.

The Tories have pinned their flag to lower taxes but haven't been able to actually do much to cut spending. There is, however, a genuine review of spending options going on inside the civil service. One of the main targets is local governments. Already there's a planned statute to limit the taxes they can impose. Although the act has no provision for reducing the functions of local governments, it would at least put a ceiling on local tax increases.

The trend toward privatization continues. Proceeds from denationalized state-owned industries and real estate are forecast to bring in about $12 billion in the next three to four years, up from $3 billion brought in during the first Thatcher term. Slated for privatization soon are 51 percent of British Telecom, the telecommunications monopoly; the British Airports Authority; the Royal Ordnance factories; and British Airways.

There is much discussion of selling government-owned real estate. Michael Osborne, an analyst with a London stock brokerage, estimates that real estate sales alone could bring in some $405 billion—enough to finance the government's deficit through the year 2010.

Meanwhile, the *Economist* has been urging that the Tories "have the courage of their radical-right convictions" when it comes to privatization. A British Airports Authority memorandum recently argued for selling its seven airports as a single unit, because this would preserve cross-subsidization of unprofitable airports by the profitable ones. But "cross-subsidization is exactly what recompetitioning in Britain should not tolerate," argued the *Economist.*

Likewise, the magazine warned against merely selling shares in government-owned enterprises. "A British Gas or British Telecom with half its shares held by the public, will merely be a partly state-owned public monopoly.... Britain would be reinventing the sort of public utility concept that Americans have been trying to bury since 1940." For the benefit of consumers, urged the *Economist*, state monopolies should be broken up and barriers to entry into a market, such as telecommunications, removed.

Similarly, local governments should not keep barriers to entry in place when they privatize garbage collection and hospital laundry service by awarding exclusive franchises, thus installing a private monopoly in place of a government one. "It should be made as easy for households to pick their own rubbish-collector as it is to pick their milkman," the magazine said.

So the political sea-change is not free of problems, but it's become an established option in the British mind to go the private route on many things.

—EBEN WILSON

CAPITALISM BY ANY OTHER NAME...

HUNGARY—Issuance of corporate bonds, proposals for stock markets, political elections with competing candidates, and widespread small-business enterpreneurship are not terribly unusual—except that they're cropping up in Hungary.

After coordinating the Soviet invasion that crushed the popular Hungarian uprising in 1956, Yuri Andropov, the wily Soviet ambassador to Budapest at the time, engineered the installation of Janos Kadar as Communist party chief. It was an inspired choice. Kadar was and still is absolutely loyal to Moscow, but he is also a little more temperate than other Eastern European dictators.

Under Kadar, there have been no more large-scale revolts, and Hungary has remained a steadfast member of the Warsaw Pact. But from Moscow's standpoint, there is a price for this stability—a series of Hungarian deviations from Communist orthodoxy.

A recent *Los Angeles Times* article

(Continued on p. 20)

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as telephone reservation operators for Best Western International. Fifty inmates at the Kansas State Penitentiary are manufacturing various sorts of metal products for a private firm. Some 40 inmates in Nevada are producing brooms for a company, while 20 others are making satellite dish antennas for another firm. And about 150 inmates in other facilities around the country are producing various commodities for sale to private companies.

Most of the inmate workers are paid the minimum wage, and in some states—Kansas, for one—deductions are taken to reimburse the state for at least part of the expense of maintaining that prisoner. A major impediment to such programs spreading to other of the nation's prisons, however, are federal and state laws—backed by organized labor, which doesn't like competition from inmates—that restrict or prohibit the hiring of inmates as well as the sale of prison-made goods.

In an article in a recent issue of *Nation's Business*, Supreme Court Chief Justice Warren Burger suggested that such laws be repealed so that the nation can turn its prisons into "factories with fences around them." (Legislators in Michigan and California are now considering revising their state laws to allow inmates to sell their labor.) Not only would prison factories teach inmates the skills to support themselves legitimately outside of prison, Warren noted, but having prisoners pay for their keep also relieves taxpayers of a considerable burden (the average cost of keeping an inmate in prison for one year: $17,000).

While the idea of inmates working for private employers increasingly appears to be taking hold, another innovative notion is emerging as well: private prisons. Already, a number of federal and state correctional bureaus are contracting with private firms and agencies to operate some of their detention facilities and halfway houses. The Federal Bureau of Prisons, for instance, contracts out the operation of all of its 300 or so halfway houses, as does Connecticut's Department of Corrections.

And one recently formed firm—Corrections Corp. of America, some of whose backers are affiliated with Hospital Corp. of America, the nation's largest for-profit hospital company—is seeking contracts with state governments to operate entire systems of minimum-security prisons. At this writing, no contracts had yet been announced.

Of particular interest, however, is the possibility of private firms financing, constructing, and operating their own correctional facilities. One firm, South-West Detention Facilities, has actually done this. It has its own jail in Johnson

GLOBAL TRENDS

(Continued from p. 18)

reviewed some of the capitalist-like reforms firmly in place or under serious discussion in Hungary. For instance, an estimated 300,000 Hungarians are in business for themselves or in partnership with friends. Some 50 enterprises are being run, on an experimental basis, by "boards of directors" made up mainly of employees. Under study are several proposals for what amounts to a stock market. A proposed constitutional tribunal would permit some institutions to challenge government decisions. And in the next parliamentary and local elections, the Communist Party will run (typically, by decree) at least two candidates for every office.

As an example of the special economic atmosphere in Hungary, the *Times* described what happened when the Vineyards Agricultural Cooperative in rural Nagyrede recently ran short of cash for expansion and modernization. It couldn't get government money because of an austerity program, and bank loans would require 14 percent interest—so the cooperative issued what Westerners call bonds. About 500 townspeople and members of the cooperative bought $230,000 worth of the bonds for a promise of 9 percent interest and full repayment by the end of 1988.

In the face of all the evidence to the contrary, Hungary's leaders go out of their way to declare the nation's continuing allegiance to socialism. "The Hungarian national economy is socialist," Kadar declaimed in a radio address last spring. "The methods applied in economic life promote the building of socialism and serve its interests. The party as well as our allies should have a clear picture of this."

Kadar and his underlings are in fact on a tightrope. There has been grumbling over the reforms from more-orthodox Communists in Eastern Europe. Moreover, Hungary has serious economic problems, including a foreign debt per capita that even exceeds Poland's.

Yet according to the *Times*, the Hungarian Communist leadership doesn't see any alternative to the path they've turned down. They've progressed to a point where, as party economist Ferenc Havasi said in an interview, a return to the old centralized system "is as inconceivable as going back to the Stone Age."

RADIO-FREEING EUROPE

FRANCE—The French government recently authorized the use of the FM radio band for broadcast by nongovernment stations, which breaks with the longtime policy of a state radio (as well as TV) monopoly. About 800 newly authorized radio stations will broadcast in this spectrum. Though the stations are prohibited from airing commercials and are under some public-interest restrictions, they are free to fashion their own fare.

By authorizing the new stations, France effectively obviated a problem that has been a headache to many European governments set on monopolization of the air waves—so-called pirate stations, or illicit broadcasters. The number of pirate stations varies from country to country—largely depending on how strongly the government monopoly is enforced. In Holland, for example, there are an estimated 10,000 pirate stations, while in Britain, where the government is cracking down hard on pirates, there are perhaps 45 of the illicit broadcasters.

In the Republic of Ireland, where some 70 or so pirate stations operate, the government has taken a course between France's liberal policy and Britain's get-tough stance: it has provided for the licensing of 30 nongovernment stations, but licenses are limited to five-year periods. And though the stations will be required to help fund certain public-interest activities in the communities where they operate, and more-lucrative stations will be required to subsidize poorer ones, the "free" stations will be allowed to sell commercial air time.

County, Wyoming, and the firm has built at least two other jails, in Rio Grande County, Texas, and in Weston County, Wyoming. And the El Paso County (Colorado) Jail Task Force has recently recommended to the county commissioners that the county contract with South-West to finance the construction of a new jail and to operate the facility. After 10 years, the county would have an option to buy the jail from the firm. At press time, the county commissioners had not yet made a decision.

One obstacle standing in the way of such arrangements is that regulations in some states may prohibit local governments from contracting with private firms to operate jails. Texas passed a bill in 1983 to allow such contract arrangements, and parties in Colorado are reportedly now drafting similar legislation. If Colorado's El Paso County decides to go ahead with the private jail plan, it will have to wait for a change in state law, which is likely to be some time in coming.

The day when all correctional facilities are built, owned, and operated by private firms—who compete in the business of caring for and rehabilitating prisoners—is a long way off. But there are signs pointing in that direction.

SHOT IN THE ARM FOR HOSPITALS

A tangle of bureaucratic regulation in California came to an end recently when the legislature passed and Gov. George Deukmejian signed legislation that removes a significant amount of the state government's regulation of hospital construction.

The scope of the regulation had been broad and deep. Before hospitals could begin construction or remodeling, they had to make their way through a labyrinth of red tape to receive a state license. The purpose of such a system, not unique to California, is to avoid the building of "unnecessary facilities" and to make sure that the ones that are built are efficiently sized and located.

The state license is called a "certificate of need." To determine need, California had devised a formula based on the number of hospital beds it deemed appropriate for its arbitrarily established "health planning districts." Also, it somehow figured "community support" for a new hospital into its calculations.

The entire idea was silly from the start. As the Orange County *Register* noted, it is presumptuous for state bureaucrats to be deciding for private investors whether a hospital should be built or expanded. "Given the immense capital investment a hospital entails these days," noted the *Register*, "it is inconceivable that such factors as need and efficient use of resources can be ignored by the private hospital developer. . . . Why cannot the market be trusted to establish the need? Why is it that state bureaucrats can do a better job?"

Fortunately, the powers that be in Sacramento have agreed, to some extent. The new legislation provides that nearly all projects in certain categories are exempt from state review, including: capital expenditures for existing health facilities; projects for remodeling, replacing, or modernizing of existing health facilities on the same or adjacent sites; and acquisitions of diagnostic and therapeutic equipment.

Moreover, in those instances where certificates of need are still required, such as the construction of new hospitals, they will be much easier to obtain,

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Derek Pogson of the Statewide Health Planning and Development Office told REASON. Before the new law, both a local hearing and Sacramento hearing were required, but only the Sacramento hearing is necessary now. And there is now a maximum waiting period of 90 days before developers are informed whether the state approves their project.

State regulation of hospitals has not ended completely. Much of the regulatory machinery is still intact. But it appears that the Deukmejian administration considers the new law the first step toward deregulation of the hospital industry. As Larry Meeks, director of the health planning office, told the *Los Angeles Times*, "The administration believes that we should deregulate and let market forces work in the health care environment."

NEW MARKET IN SATELLITE SERVICES?

The days of Intelsat's 18-year governmental monopoly in transatlantic communications satellites may well be numbered. The consortium of 109 nations, which operates 16 satellites, has been challenged in recent months by two private companies—International Satellite, Inc., and Orion Satellite Corp. Each firm wants to launch two communications satellites in 1985 or 1986 to relay signals between the United States and Europe, and they have asked the Federal Communications Commission for permission to do so.

It's no secret that Intelsat does not welcome the new private-sector competition. It's easy to see why. Intelsat's satellites brought in $310 million in 1982, and revenues are expected to skyrocket to $600 million by next year.

Of all the Intelsat members, none has a greater stake in maintaining monopoly revenues than Comsat, the American representative. It owns 24 percent of Intelsat and, according to *Business Week*, derived $250 million of its $409 million operating revenues in 1982 from resale of Intelsat's phone circuits. Such are the little blessings of state-sanctioned monopoly.

Intelsat and Comsat are jealously guarding their turf. An article in *Aviation Week* noted that Intelsat has determined that regional satellite networks would threaten its viability if international or transoceanic traffic is diverted from its present system. Already, Comsat has filed a petition with the FCC to deny upstart Orion's application.

At this writing, it's too early to tell whether the FCC will grant the applications of International Satellite and Orion or be deflected by the Intelsat and Comsat monopolists. Christopher Vizas, an attorney and co-owner of Orion, told REASON that the FCC will pay close attention to the Reagan administration's position, currently being developed by the State and Commerce departments—but that isn't expected to be announced until late January or February at the earliest.

In any event, there are already benefits to the private-sector challenge. A nervous Intelsat is going so far as to offer new kinds of service. For example, customers can now install their own antennas and beam messages directly to an Intelsat satellite.

Perhaps the monopoly sees the writing on the wall.

LESS WASTE WITH PRIVATE COLLECTION

Garbage pick-up by Canadian municipal crews is an average of 51 percent more costly than collection by private crews. Even when factors such as service levels, environment, and technology are controlled for, the municipal service still costs 35 percent more. Those are two of the findings of a Canada-wide study recently concluded by Jim McDavid, a professor at the University of Victoria's School of Public Administration in British Columbia.

Part of the reason for private crews' lower costs: they are more productive. Even with smaller crew sizes, found McDavid, private haulers collect more tons of waste per crew-hour than do the municipally employed crews. Private companies' superior technology—the use of newer, more-efficient equipment—and built-in incentive systems in part account for the private firms' better performance, but McDavid plans further research to give more-precise reasons.

Private garbage collection appears to be a growing trend in Canada. For example, 91 percent of Montreal's waste-collection services are provided by private firms, and recently two communities in the Vancouver area contracted out their garbage collection to private companies.

McDavid, in follow-up research to his study, is examining the cases of three Canadian cities that within the last two years switched from municipal to private garbage collection. The results, we expect, will add yet another layer of evidence in the case for privatization of municipal services.

MILESTONES

• *Pipeline plugged.* By a 53-vote margin, the House of Representatives in September defeated a bill that would have given builders of coal-slurry pipelines eminent-domain power to acquire rights of way for the pipelines.

• *Phone rules relaxed.* Since mid-October, long-distance phone-service rivals of AT&T no longer need permission from the Federal Communications Commission to change their rates, nor do they have to justify rate increases any longer. AT&T, which is still subject to the rate-filing and -justification rules—until the FCC figures out what to do about deregulating the phone giant—called the FCC's exempting it from the rule changes "an incredible action."

• *Clinch nuked.* The Senate has dealt a death blow to the controversial Clinch River Breeder Reactor. By a vote of 56 to 40 in October, it voted to cease further subsidies for the multi-billion-dollar project, thereby giving it the coup de grace (approval by both houses was required).

• *Merit, not race.* The B'nai B'rith Anti-Defamation League has released a survey indicating that 73 percent of Americans believe that hiring should be based on merit, not race or ethnicity.

• *Consenting sex deregulated.* Wisconsin has enacted the "Clarenbach bill," legislation sponsored by Rep. David Clarenbach that eliminates criminal penalties for cohabitation, fornication, homosexual acts, and other sexual behavior between (or among) consenting adults in private.

• *Se habla ingles.* Criticizing much "bilingual" education as lacking "any genuine effort to help [children] function in English as soon as possible," the editors of the *New York Times* in September endorsed a Reagan-administration proposal to allow local school districts to determine how best to teach English to non-English-speaking children. The editorial referred to a Twentieth Century Fund study urging an end to federal support of bilingual instruction.

—ROBERT W. POOLE, JR.,
PAUL GORDON,
AND ERIC MARTI

The Sleeping Giant Wakes: Resurgent Populism and the Break-Up of the Democrat-Republican Status Quo

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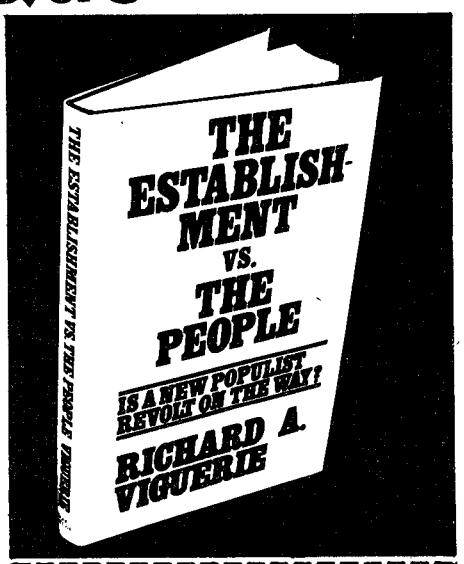

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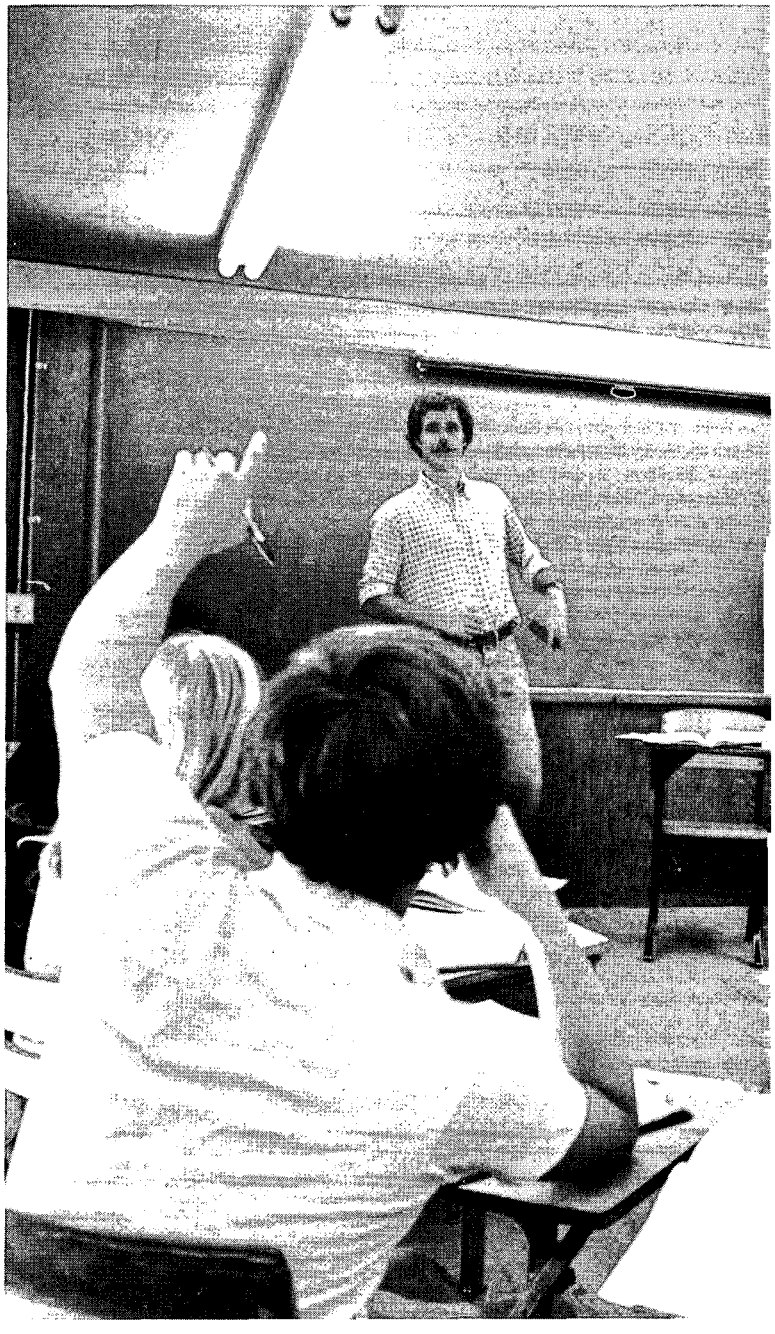
By John McClaughry



Tracy and Jesse Torregrossa are the children of a pharmacist in Dorset, Vermont, located in the southeastern part of the state. This fall, Tracy started her senior year at Proctor School in New Hampshire, and Jesse began his third year of high school at Hebron Academy in Maine. Meanwhile, in the northeast corner of Vermont, Anna McClaughry is reading Shakespeare in the fifth grade at Riverside School, located in an old farmhouse near Lyndonville.

Proctor School, Hebron Academy, and Riverside School are all private institutions. There's nothing unusual about that. What *is* unusual about the education of these three children is that their families live in Vermont school districts that in effect offer tuition vouchers to some or all of their pupils. The Dorset School District pays about a third of the private-school costs for the Torregrossas, and the town school district of Kirby pays the entire $1,750 annual tuition for Anna McClaughry's schooling.

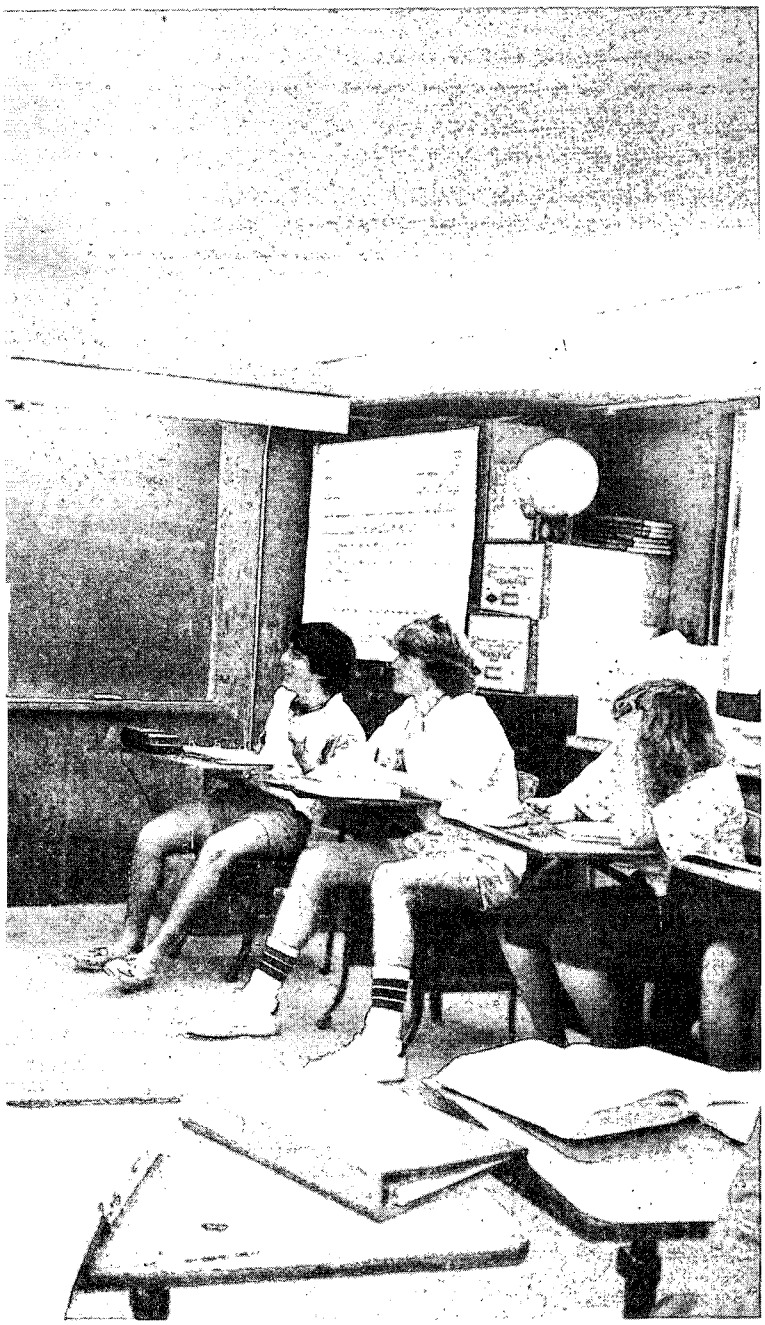
This is extremely unusual in the United States, and it's more than a little ironic. Washington bureaucrats, Chicago free-market economists, Harvard sociologists, and teachers-union officials from New York to California have argued for years over the idea of education vouchers, even seeing a much-ballyhooed but ill-fated "voucher experiment" come and go in the 1970s. Meanwhile, students in almost 100 Vermont towns have quietly received education vouchers from their local school districts, just as their parents and grandparents did before them.

Now Vermonters have never used the word *voucher* to describe what happens there, and some state officials were kind of skittish about a reporter coming around and asking questions. Nevertheless, long before the rest of the country had ever heard of the idea, many Vermonters were benefiting from a system whereby the local government uses tax monies to pay for education rather than to provide it.

Early Vermonters, like all New Englanders, placed great value on the education of their children. Vermont's 1777 constitution—the oldest state constitution still in force—provided that "a competent number of schools ought to be maintained

PHOTOGRAPH BY BILL ZELDIS

Wouldn't Work?



in each town unless the General Assembly permits other provisions for the convenient instruction of youth." Citizens then undertook to found private academies to educate their sons and daughters. People's Academy in Morrisville, Bellows Free Academy in Fairfax, and Burr and Burton Seminary in Manchester are typical survivors from this early era.

As the idea of universal taxpayer-supported education took hold in the first part of the 19th century, the future of these local academies was questioned. Should the local school district finance a new public high school, thus dooming the local private academy? Or should the district simply pay tuition to the private academy, which would serve the purposes of a local public high school?

Since the prominent civic leaders of most Vermont communities had themselves graduated from local private academies, they usually exerted their influence against putting the school out of business by creating a new public high school. Taxpayers also were generally averse to the idea, since it was obviously cheaper for the school district to pay tuition for their children than to assume the capital costs of creating a whole new school. And so it became a tradition in many Vermont towns simply to have the taxpayers pay for the town's children to attend the local private academy. Where there was no private academy, the local school district created and supported a public high school or joined with nearby towns to create union districts. In a few cases, like Townshend's old Leland and Gray Academy, the private school was converted into a public high school.

Vermont's experience was not unique. Headmaster James Steenstra of the Gilbert School in Connecticut says that, beginning in the early 1800s, local governments throughout New England financed the education of school children at private academies. Today, vestiges of the system remain in three towns in rural Connecticut (Norwich, Winsted, and Woodstock) and at least three towns in Maine (Lee, Blue Hill, and Dover-Foxcroft).

Today 95 of Vermont's 246 towns have no public high school and do not belong to any of the state's 27 union high school districts. State law authorizes the school boards of these towns to designate a high school and to pay the full tuition for any local student to attend it. If a school district does not designate a high school, it must pay on behalf of any town pupil, to any approved high school in or out of the state, a tuition amount equal to the average Vermont union high school tuition ($2,675.67 in the 1983-84 school year). If tuition at the chosen high school exceeds that amount, the school district may choose to pay the full amount, but because of taxpayer pressure this is rarely done. The parents must chip in the difference.

Even if the local school district designates the local private academy as the town's high school, it may still be possible for parents to enroll their children elsewhere with voucher support. The town of Lyndon has a strict policy. It has designated Lyndon Institute as its high school and stoutly resists parents' request to send their children elsewhere. The reason cannot be economic, for the Lyndon Institute tuition is slightly above the state union average. The school board seems to believe that all local students simply should attend the local high school. On occasion, presented with a very strong argument, it has relented, but more commonly it will deny appeals. The state Board of Education has upheld the denials.

St. Johnsbury, nine miles from Lyndon, has the opposite policy. Rather than designating St. Johnsbury Academy as the official high school, the authorities allow parents to choose any approved school. But of the 419 high-school-age students in

the district last year, 401 did attend St. Johnsbury Academy. Seventeen chose other nearby schools; only one student attended private school away from the area (in Connecticut). Since St. Johnsbury Academy's tuition is $465 above the state union average and the district chooses to pay the entire tuition, one would think that taxpayer pressure would encourage parents to select alternative schools—but this does not seem to be the case. St. Johnsbury Academy, with an excellent scholastic and athletic reputation, has long been the preferred choice of local parents. It also has a boarding department for approximately 40 additional students from elsewhere.

The Manchester-Dorset area, where the Torregrossas live, has a relatively high-income, well-educated population, famous for expensive summer homes and country clubs. According to state records, the two towns together had 344 high school pupils last year. Of these, 299 attended Burr and Burton Seminary, a nonsectarian private academy located in Manchester. Three attended public high schools in Vermont or nearby New York. Seventeen chose private schools elsewhere in Vermont. The remaining 15 attended out-of-state private schools from Phillips Exeter to Lawrenceville to Miss Porter's School. One of them ranged as far afield as Ketchum School in Idaho. To each school the Manchester or Dorset school district supplied a check for $2,480.20, the state-designated average for 1982-83. This covered 25-35 percent of the tuition, room, and board costs for such high-class private academies. Parents, of course, made up the difference.

Barre Town, a blue-collar rural area surrounding industrial Barre City and Vermont's famous granite quarries, presents an entirely different picture. Of the 594 high school pupils in Barre Town last year, 521 attended public high school in Barre City. Another 72 went to public high schools in nearby towns, presumably for geographical reasons. Only one went to a private secondary school in a nearby town.

There is an important limitation on the voucher system. Payments can be made only to nonsectarian private schools approved by Vermont's Department of Education. This at once leaves out the state's three Catholic high schools and one fundamentalist Christian school. The department maintains a list of approved schools, which includes most of the established private academies in New York and New England. When parents propose to send a child to a school not on the list, the department will investigate. For well-established schools, a call to the department of education in the other state may suffice. In some cases the Vermont department will dispatch a field investigator. According to department officials, in one recent case the school was not approved, and the parents, informed of the reasons, chose another private school. Ordinarily, there is some presumption that parents who can ante up $5,000 above the value of a voucher should have some idea of what they are buying.

My own town of Kirby, population 285, is one of about 25 Vermont towns that has a voucher system for all grades, not just for high school. Kirby, which reached its peak population of about 500 in the late 19th century, once had six separate school districts. In living memory there have been five operating one-room schools in the town. In 1978 the townspeople voted to close its last school, which had only 11 pupils in grades one through six. (Although there are enough children in the town to support a one-room school, their geographical distribution means that there is no convenient place to locate such a school.)

So, since 1978, taxpayers have paid the full tuition for Kirby's grade-school children to attend school in adjacent towns (and at least the state union average for high-school pupils). The town continues to pay for two school buses to transport most of its pupils to the schools of their choice, although some must arrange their own transportation.

Among the available schools is Anna McClaughry's. Three years ago a private grade school in Newark, 18 miles from Kirby, closed its doors when the proprietor decided to take a sabbatical. Some of the suddenly unemployed teachers and the parents of the pupils founded Riverside School, located on the Kirby side of nearby Lyndon. The school offers instruction in grades 5-8, emphasizing literacy, the mastery of traditional subject matter ("social studies" has been banned), French and Latin, environmental appreciation, and computer knowledge. In contrast with most public middle schools, three of its six teachers hold degrees from Yale, Harvard, and the Sorbonne.

Five of the "orphan" Kirby pupils are attending Riverside, their full tuition of $1,750 paid by the taxpayers via the Kirby school board. (Parents of the remaining 21 pupils, who come from towns that maintain public grade schools, must pay the tuition themselves.) Headmaster Richard Koehne told REASON that he is very pleased to have the Kirby pupils, noting that the town's voucher system creates more potential customers for his school. "We especially like having kids come from Kirby on the voucher plan because it broadens our student body mix," he says. "Otherwise, we would have only children of parents who could afford the tuition on top of the property taxes they pay to support the public schools."

While bureaucrats, economists, teachers-union officials, and sociologists still argue about vouchers, 95 Vermont school districts have had them for generations.

While Vermonters, unbeknownst to the rest of America, have been carrying on their voucher-like tradition, a debate about vouchers has been part of a growing movement in the country to change public policy so that more parents will have a meaningful choice about their children's education. The reason for this movement, as Harvard law professor Charles Fried aptly summarized recently in the *New Republic*, is that "many individuals are deeply dissatisfied with the public education system and the network of union and political alliances that make it particularly hard to change."

Parents have traditionally had the option, of course, of sending their children to private schools. This option was threatened in Oregon early in this century when the state legislature passed a law requiring attendance at government-operated schools. Fortunately, that law was struck down by the US Supreme Court in 1925. Justice James McReynolds, speaking for a unanimous Court in *Pierce* v. *Society of Sisters*, declared that "the fundamental theory of liberty upon which all governments in this Union repose excludes any general power of the state to standardize its children by forcing them to accept instruction from public teachers only. The child is not the mere creature of the state; those who nurture him and direct his destiny have the right, coupled with the high duty, to recognize and prepare him for additional obligations."

The *Pierce* case ended the legal threat to the existence of private schools, but parents who desired private education for their children have still faced the problem of cost. There is no exemption or rebate from the various taxes used to support

public education. And thus nonpublic education has been the province either of the affluent, who can afford to pay both bills, or of parents whose church—notably the Roman Catholic and Lutheran—has managed to offer parochial schooling at less than its true cost.

The double burden is not insignificant. The Census Bureau figures that total expenditures for elementary and secondary schools in the 1980-81 school year had to be funded by $444 in taxes per man, woman, and child in the United States. So a couple with two children was paying $1,776 in taxes to support the public school system that year, regardless of whether their children were actually attending government schools. If a family chose to send their children to private schools, they would pay, in addition, around $400 a year for church-affiliated elementary schools and $1,500 for other private elementary schools; private high schools cost even more.

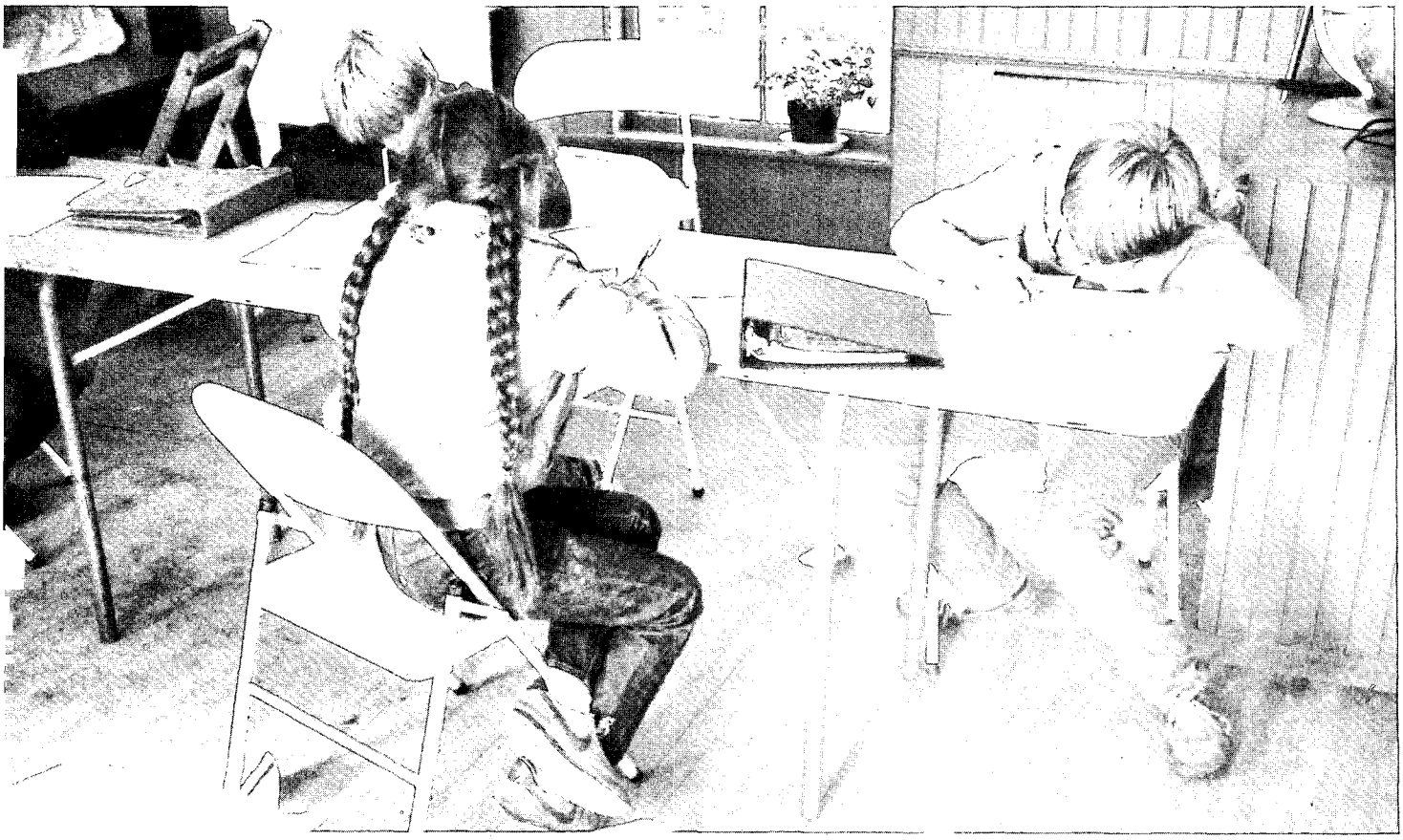
In the late 1940s, the hierarchy of the Catholic Church made a serious push in Congress for government aid to parochial schools, triggering a spirited church-state controversy that ended in the proposal's defeat. Over the next 20 years, however, a new proposal emerged from three quite different quarters. Called the "tuition voucher," it provided for government grants directly to parents, who could then use the proceeds to purchase education for their children from the school of their choice, whether public or private.

An early and eloquent advocate of tuition vouchers was free-market economist Milton Friedman. In 1962, in his influential *Capitalism and Freedom*, Friedman stood the time-honored argument for public education on its head. Do public schools produce a healthy mix of rich and poor, black and white, etc.? Perhaps in the days of the small town with only one school, but not with the rise of populous urban and suburban areas that are economically and racially stratified. A poor black urban family, Friedman pointed out, could possibly save its money and buy the same fancy car owned by a well-to-do white suburbanite, without also buying a fancy house in the suburb. But it was highly unlikely that the black family could afford to send its children to first-class schools located far away from the lower-income black neighborhood. (And a recent study by the National Institute of Education suggests that, after two decades of efforts at integration, minority parents are in the same position today.)

How could a system widely regarded as incompetent, overcostly, and perhaps unjust be most improved? Some people favor an end to all state involvement in education, but that is "outside the range of political feasibility today," Friedman wrote in a 1973 *New York Times Magazine* article. In an essay published in 1955, however, Friedman first wrote of vouchers, saying that they would "give competition and free enterprise greater scope" and "pave the way for the gradual replacement of public schools by private schools."

For most of America this was a startling new idea, but Friedman's proposal was close to the system already in place in some Vermont districts. He would have local school boards provide parents of every school-age child a voucher for an amount equal to the average cost of educating a child in the local government schools. The parents would "be free to spend the voucher and any additional sum they themselves provided on purchasing educational services from an 'approved' institution of their choice," Friedman explained a few years later in *Capitalism and Freedom*. "The role of government would then be limited to insuring that the schools met certain minimum standards, such as the inclusion of a minimum common content in their programs."

Friedman emphasizes that parents should be able to use their vouchers in both private and government schools, whether in the school district or not, if the schools are willing to accept the children. This, he argues, would give parents real



For some students at Vermont's Riverside School, a private academy, vouchers cover the annual tuition of $1,750.

PHOTOGRAPH BY GERRY STORK

freedom of choice, encourage healthy competition among schools, and inject a market standard for teachers' salaries.

Nothing came of Friedman's proposal at the time, but others began to think along the same lines. Christopher Jencks, a liberal professor of education at Harvard University (now at Northwestern University), advocated a voucher system as early as 1966. In 1970 he argued that vouchers could meliorate the plight of black children in underfunded and ineffective ghetto schools. Since despite a decade of civil rights agitation and progress, it did not appear that black schools in white-dominated cities would ever be brought up to the level of the better white schools, Jencks favored vouchers to allow blacks to attend the white schools instead of the schools nearest their homes.

Meanwhile, a few Catholic educators were warming up to the voucher idea. Unlike the earlier proposal to divert tax monies directly to parochial schools, the voucher plan ostensibly subsidized parents, just as the post-World War II GI Bill had subsidized students. It would then be immaterial whether the parents cashed their vouchers with parochial schools or nonsectarian private schools or public schools. Inasmuch as the earlier GI Bill had stimulated a wave of trade schools created expressly to relieve veterans of their GI Bill dollars,

Economist Milton Friedman: Vouchers could pave the way for the replacement of public schools by private schools.

LESSONS FROM ABROAD

The principle behind vouchers—privatizing decisions on where and how children are educated—is firmly established to varying degrees in several countries. Estelle James, chair of the economics department at the State University of New York at Stony Brook, told REASON that in a number of countries, including France, Great Britain, Norway, and India, governments finance part or all of children's education in nongovernmental schools. However, no other systems are as close to the voucher idea as in the Netherlands and in British Columbia.

James did a study of the Dutch system for the Institution for Social and Policy Studies at Yale. She observed that the Dutch arrangement, in existence since the late 19th century and codified in the nation's 1917 constitution, is "much like a voucher system, with strings attached."

Each family gets a voucher that is equivalent in value to the per capita cost in the local public school. It must be spent on education. The school that receives the voucher is then entitled to funding to cover specified amounts of teachers' salaries and other expenses.

It is not exactly a free market. The private schools' right to raise and spend funds as they see fit is limited. According to James, schools have some discretion to charge parents ancillary fees in addition to the voucher, usually between $100 and $200 a year. A new law took effect last year saying that parents' failure to pay ancillary fees cannot be grounds for excluding a child from a private school—but this is expected to have little effect, since most schools traditionally waived ancillary fees for low-income families.

There are other state regulations. For example, the central government pays all teachers' salaries directly, and these salaries are determined by fixed schedules based on education and experience. Schools may not supplement these salaries.

Such intrusions may be substantial, but James observed that private schools in the Netherlands still have wide latitude to operate very differently from government-run schools. And some 70 percent of Dutch parents send their children to private schools, indicating that private schools are preferred by consumers.

In discussions with parents and educators, James discovered a widely held belief that private schools:
—"are more personal [than public schools] and responsive to parental wishes,"
—"spend funds more effectively and use their fees to secure better facilities," and,
—"label their ideology ahead of time, so parents know what they will be getting, in contrast to public schools which ostensibly have no ideology except that which the individual teacher adopts."

Secular private schools certainly exist in Holland, but about 95 percent of voucher-eligible schools are church-related, most commonly with the Dutch Reformed, Calvinist, or Catholic churches. It is relatively easy to start a voucher-eligible private school in Holland. The 1920 Law on Education requires only that parents of a specified number of students join together in a formal organization and request a school with a specific religious or pedagogical philosophy. Currently, the minimum number of participating families varies from 50 in the smallest municipalities to 125 in the largest.

In British Columbia, a voucher-like system has been in place since the 1977-78 school year. Only six years old, it is less extensive than the Dutch system but is considerably closer to free-market principles.

As in the Netherlands, there is no voucher form per se. At the end of each school year, British Columbia's independent (private) schools that qualify receive aid

this contention was somewhat transparent; but the movement still grew.

During this period, however, the opposition was far from asleep. Advocates of public schools saw that a movement toward vouchers would threaten their effective government monopoly over education. Local school boards and superintendents didn't like the proposal. Teachers unions particularly opposed the idea, it being easier to organize a relatively small number of large public-school systems than a large number of small private schools. In addition, as Friedman had argued, the teachers recognized that a real marketplace for education would mean competitive pressure to hold down their salaries. So the National Education Association and the American Federation of Teachers began to allocate substantial resources to heading off the voucher scheme.

Indeed, vouchers probably have no more passionate enemy than Albert Shanker, president of the American Federation of Teachers. For years, Shanker has written a column published as a paid advertisement in the *New York Times*, and several have been devoted to lambasting vouchers.

In 1971, Shanker wrote, "The greater the free choice granted by a voucher plan, the more will the educational interests of poor, black and difficult children suffer." (Never mind that "poor, black and difficult children" under the current system are ordinarily the ones with the least possibility of affording private alternatives to inferior government schools.)

Teachers-union chief Albert Shanker: Voucher schools would compete like toothpaste companies and department stores.

directly proportional to the number of students they have enrolled. But unlike the Netherlands, there is no government regulation of teachers' salaries nor of participating schools' right to charge parents additional tuition and to solicit contributions.

There are two groups of independent schools eligible for support. A school in the first group needs to meet relatively lenient standards: adequate facilities, three years in operation as a nonprofit society (equivalent to a nonprofit corporation in the United States), and no programs that "promote or foster doctrines of

Under a voucher system, some 70 percent of Dutch parents send their children to private schools.

racial or ethnic superiority, religious intolerance or persecution, or social change through violent actions."

A school in this group receives, for each of its pupils, an amount equal to 9 percent of the average operating costs per pupil in the public schools. The independent school can then use these funds for "peripheral services" such as student transportation and textbooks.

The second group of schools must comply with more stringent regulations governing curriculum, pupil testing, program assessment, and teacher certification, in addition to the first group's qualifications. However, it receives, for each pupil, 30 percent of the average operating costs per public-school pupil (that 30 percent was $954 in 1982-83).

The provincial government is very straightforward about the rationale for the aid program. Education Minister Jack Heinrich wrote in an open letter last September that it "relieves taxpayers of costs far in excess of the subsidy [the schools] receive."

The current student population in British Columbia is 487,000, according to a ministry official. Of these, 23,500 are attending the province's 140 independent schools that receive aid (another 6,000-7,000 are in independent schools that don't qualify for aid—mainly fundamentalist Christian schools).

The aid plan's enabling legislation in 1977 sparked considerable controversy. The relatively conservative ruling party, the Social Credit Party, was supportive, while the socialist New Democratic Party was generally opposed. Now, however, a ministry official notes that "people are treating it as permanent." Even the New Democrats, who are out of power, have pledged to retain the program if they win office.

Statistics indicate that the aid program is working quite well. As might be expected, learning assessments comparing the independent schools to the public schools consistently indicate the independent schools' superiority. But it's also interesting that the average family income of independent-school students is slightly lower than the provincial average, probably because of the heavy representation of urban working-class Catholics. This has been somewhat embarrassing for early critics of the aid program who claimed that it smacked of elitism.

Another interesting phenomenon: Stephen Easton of Simon Fraser University, an expert on aid to private education, told REASON that although hard figures aren't available, he has observed a migration of teachers from the public school system since the voucher law was passed. Apparently they're turning entrepreneur and setting up independent schools despite the lower level of government funding there.

"When people in the United States talk about vouchers," Easton told REASON, "they're thinking of Alum Rock. If they want to see a real experiment with vouchers, all they have to do is to look right across the border."

—P. G.

"Our public schools...are designed to keep our society together," he opined in 1979. "Vouchers are designed to use tax money to pull our society apart." (Never mind that the all-important purpose of schools is educational, not social, and that in this purpose they have by wide agreement failed miserably.)

And in a 1980 column: "There would be competition among schools in much the same way as there is now competition among toothpaste companies, auto manufacturers and department stores. Some enterprising schools might offer gifts to newly enrolling students in much the same way that savings banks offer such gifts to new depositors. Or...students might be offered rewards for enrolling their friends!" (Never mind that precisely such competition has resulted in largely satisfied toothpaste, auto, and department store customers.)

In 1983, a majority of Americans in a national survey expressed support for education vouchers—but most politicians remain skittish.

Shanker and his teachers union colleagues were first mobilized by a voucher study conducted in the late '60s under Christopher Jencks's direction at the Center for the Study of Public Policy in Cambridge, Massachusetts. The authors of the study endorsed education vouchers; but unlike the simple Friedman plan, theirs included a number of special restrictions on the vouchers. For example, they recommended that local government agencies be given a mandate to:

—establish higher voucher payments for poor and mentally handicapped students;

—regulate schools' admissions and expulsions policies ("one critical notion in our report was that a voucher school should admit nearly everyone who wanted to attend, space permitting," Jencks recently told REASON); and,

—forbid parents to pay any tuition out of their own pockets to supplement their children's vouchers.

The Nixon administration's Office of Economic Opportunity (OEO), still populated with a number of Great Society bureaucrats, had supported this study. Bolstered by rhetorical support from Friedmanite libertarians, OEO began in 1970 to look for a test site for a voucher experiment. But when they broached the idea in Seattle, San Francisco, and Rochester, they ran into a buzzsaw of opposition.

Those who favored racial integration opposed vouchers because they saw in them a way out for white students, not a way in for blacks. The more OEO tried to contend with their objections, the more the anti-integration forces shied away from the idea. Church-state separationists were put off when Catholics supported the plan. Local superintendents and board members began to view the whole scheme as causing far more trouble than it could possibly be worth, especially in view of the continuing necessity for taking in enough revenues to meet long-term fixed costs for school plants. Teachers unions, as usual, were strongly and actively opposed.

Vouchers' best chance came in New Hampshire, which had no racial-integration problem and a governor and state board of education chairman who were ardent free-marketeers. They prevailed on the Nixon administration to offer New Hampshire a "free market voucher," considerably less restrictive than the "regulated compensatory voucher" urged by Jencks and the OEO liberals. Fortified with ever-increasing federal funding, OEO and the state finally got five school districts to plan for a test—until the teachers' unions let loose their adamant opposition, and all five districts backed down.

Finally OEO found a test site, Alum Rock School District, a largely lower-middle-class and lower-class area in San Jose, California, with one of the lowest assessed property valuations per student in the state. After lengthy negotiations between the agency and school district officials, a three-year demonstration project was established in 1972.

It was set up to include 6 of the district's 24 public schools. Under the plan, 22 "minischools" were formed at the six participating schools. Eleven of the minischools emphasized general basic academic skills, while various others emphasized reading, math and science, fine arts, cross-cultural learning, and learning basic academic skills through practical everyday activities.

In the spring, each school would plan its minischool programs for the next year, and descriptions of all the district's minischools were compiled and sent to parents along with voucher forms. For each child, parents indicated on the voucher form their first three choices of programs and of schools where the programs were being offered. Each student had a spot guaranteed at his or her neighborhood school ("squatter's rights"). When there were not enough spaces in a minischool to accommodate all the applicants from outside the neighborhood, the available spaces were rationed out by lottery.

A "compensatory voucher" allotment addressed a worry of Jencks and his colleagues that in a voucher system, teachers and schools would want to teach middle-class and wealthy children while ignoring poorer children. To create a greater incentive for minischools to teach poor children, the voucher amount for Alum Rock students who were eligible for the federal school-lunch program was 30 percent higher.

"Alum Rock can show the way," the *Los Angeles Times* announced in 1973. They spoke a bit too soon. On the whole, the Alum Rock experiment proved to be a fiasco. A Rand Corporation study in 1974 found that in every voucher school, in all grades but one, students fell behind in achievement while students at Alum Rock's nonvoucher schools essentially held their own. Robert Klitgaard of Rand called it "one of the starkest downward effects I've ever seen."

But the Alum Rock project was hardly a test of the voucher idea. From the start, the experiment's design was far removed from an authentic voucher plan. For one thing, private schools were effectively excluded. They were technically eligible for vouchers but had to comply with a host of district regulations concerning teacher certification, curriculum standards, student discipline, and more. For that reason, no private school ever actually received a voucher.

Also, the minischools' admissions and expulsion procedures were heavily regulated, so they had none of the freedom that private schools have to enforce strict educational and conduct requirements. Moreover, schools were given enrollment ceilings. Thus, the schools that offered the best programs, by parents' lights, could not expand to accommodate more students, and the schools in lesser demand inevitably enrolled the overflow from the more-sought-after schools. Moreover, in stark contrast to a competitive market situation, teachers who garnered few students were guaranteed a salary on the OEO payroll, while good teachers whose reputation or teaching competence attracted more students would not be rewarded with higher salaries.

VOUCHERS OR CREDITS?

One of the strongest advocates of education vouchers, Milton Friedman, argues that they will "pave the way for the gradual replacement of public schools by private schools." But many other supporters of free-market education disagree. Worrying that a voucher system might foster even greater intrusion on individual liberty than the present system does, they argue instead for education tax credits as a better way to move in the direction of privatizing education.

While some advocates of the voucher say it would reduce government control over education and foster diversity in schools, tax-credit advocates suggest that a voucher system could in fact have the opposite effect. They reason that to be eligible for voucher reimbursement from the government, private schools that are now virtually free of regulation would probably have to submit to a number of new governmental strictures.

Even some of the most modest regulatory schemes in proposed voucher systems would exclude parochial schools and racially discriminatory schools. But other, more ambitious voucher plans contemplate government regulation of private schools' admission and expulsion policies (some would deny private schools much latitude to reject or expel students), tuition schedules, curriculum, teacher qualifications, and faculty salaries.

Tax-credit advocates argue that under any voucher plan, there would be immense political pressure from school boards and teachers' unions to make schools satisfy a long list of requirements to be eligible for vouchers. To the extent that those would-be regulators were successful, a reform aimed at reducing state power in education would ironically extend it to private schools where it has been minimal or nonexistent.

Supporters of tax credits also note that with a voucher system, some taxpayers would still be forced to subsidize the education of other people's children, even more so than now. Indeed, the tax burden would probably be increased, since costs would be incurred for families of private-school students who are now paying their own way. And, as with the present system, small families and single people would bear a relatively large share of the tax burden compared to benefits received.

Thus, short of complete government withdrawal from the education industry, tax credits are often seen as a reform with greater potential than vouchers. There have been several versions of such credits, but the one that would offer the most freedom from government would be patterned on two recent initiative proposals in Washington, D.C., and California. These versions have three features that make them distinct from a proposal currently favored by the Reagan administration.

First, government authorities would be explicitly prohibited from imposing rules and regulations on schools in the name of tax credits.

Second, a credit would be allowed for paying the educational expenses of *any* student, whether related to the taxpayer or not. The credit would thus be available both to individuals and to corporations. Any taxpayer could easily help finance the education of a friend or some needy youngster who would otherwise have no opportunity to elect to attend a private school. This plan also opens up new opportunities for corporate giving as well as for employee benefits.

Finally, to avoid snags arising from First Amendment issues of church-state separation, credits would be allowed for payment of students' educational expenses at either private or government-run schools. With this feature, a carefully drafted tax-credit measure would be likely to survive challenges in court, under the authority of a 1983 Supreme Court decision upholding a Minnesota statute providing for state income-tax deductions for educational expenses at any school.

A credit could have other significant advantages over vouchers. It would implicitly recognize that taxpayers' money is their own, to be spent when and where they see fit. It would not require a coerced governmental transfer payment, as a voucher does. And practically, there would be far less rationale for government's policing schools that receive private contributions as opposed to government reimbursement.

Free-market defenders of tax credits usually agree that a voucher system would be an improvement over the status quo. They do contend, however, that an educational tax credit would be less vulnerable to statist depredations. In a free society, education should ultimately be provided on a fully privatized basis. A well-designed tax credit seems to them best calculated to move us in that direction.

—MANUEL S. KLAUSNER

Mercifully, the entire Alum Rock experiment ended in 1975. Not a single school district in the country followed its example.

As dismayed voucher advocates examined the results of Alum Rock, many were worried that this bad imitation of vouchers would be taken to reflect on vouchers generally. Certainly, confirmed voucher opponents seized on Alum Rock to try to discredit vouchers. Voucher arch-enemy Albert Shanker crowed in the aftermath, "The washout serves to remind us that panaceas sold to the public rarely work in practice."

But Shanker and company were not entirely successful. An infrastructure of intellectual and academic support for vouchers continued through the 1970s and into the '80s. The idea today is kept alive partly by the efforts of the Education Voucher Institute (EVI), a think tank in Ann Arbor, Michigan, whose executive director is University of Michigan professor William Coats.

As in the beginning with free-marketeer Milton Friedman and liberal Christopher Jencks, support for vouchers over the years has come from across the political spectrum. On the right, William F. Buckley argued for vouchers in his book *Four Reforms*; sociologist Edward Banfield endorsed them; and in the past, the Young Americans for Freedom has made vouchers a high priority.

On the left, liberal and radical advocates of education reform such as John Holt, Nat Hentoff, and Jonathan Kozol—and, less enthusiastically, politicians like Sen. Daniel Patrick Moynihan (D-N.Y.)—have come out in favor of vouchers.

Nat Hentoff, columnist for the *Village Voice* and the *Progressive*, is typical. In a 1972 magazine article, he wrote about choosing schools for his own children. "I did visit our local public school," he recalled. "The children there were being treated like automobile parts on an assembly line. So my four children are in four different private schools, because each learns in a different way."

He continued, "If I were not able to afford those four tuitions, my children would be compressed into the single mold the public school chooses for all children, and at least two of them might well have dropped out by now.... Why not allow for some real democratic pluralism in public education by ending that monopoly through making public *independent* education also possible? Consider the range of choice that would then be available to parents now restricted to the monopoly system."

Hentoff recently told REASON that he still supports vouchers if they are given to schools that do not discriminate on grounds of race, sex, etc., and if they are not given to church-related schools.

Politicians have generally been skittish about the issue of vouchers. Few doubt that it has a lot to do with the political pull of the two big teachers' unions, the National Education Association and the American Federation of Teachers.

Vouchers found a desultory champion in Ronald Reagan. While governor of California, Reagan called for vouchers in his 1972 "state of the state" message. Voucher legislation was introduced, but disappointed supporters in the legislature complained to the *Los Angeles Times* that Reagan "gave the measure little support," and it died in committee.

Last spring, the Reagan administration proposed giving local school districts the option of converting their federally funded Title I program (billed as supplemental education services for educationally disadvantaged children) to a voucher system. A bill was drafted by the administration and sponsored by Rep. John Erlenborn (R-Ill.), but history may be repeating itself. After a single day of House subcommittee hearings, the legislation faded away, and the administration has reportedly done little to promote it.

There is one state government where vouchers may be getting a fair hearing. Rep. John Brandl (D) has introduced a bill in the Minnesota legislature to provide vouchers worth $1,475 per pupil for low-income families. The vouchers would be good at any school. Minnesota's Democratic governor, Rudy Perpich, is reportedly "committed to the market-based system" in education but has not yet endorsed the legislation (see Trends, Aug. 1983). Minnesota has already instituted a tax deduction for education expenses, and the measure survived a legal challenge on church-state grounds when the Supreme Court recently upheld its constitutionality.

Elsewhere, voucher advocates who have not met with success in state legislatures have turned in some instances to the ballot referendum. The first major campaign of this sort was in 1978 in Michigan, which lost by 59-41 percent.

Perhaps the most ambitious campaign came in California two years later. John Coons and Stephen Sugarman, two liberal Berkeley law professors, drafted a ballot initiative that would have set up a two-part voucher—a base amount allocated for all students no matter what their family income and a supplementary amount proportional to their family income.

Coons and Sugarman's "Family Choice Initiative," as it was called, was hotly debated in late 1979 and early 1980. As could have been predicted, the state's educational establishment was bitterly opposed. Wilson Riles, then the state superintendent of public instruction, stormed, "The idea is crazy....I see chaos [if it passes]." In the face of this opposition, the initiative was unable to gather sufficient signatures for ballot status.

An interesting coalition of liberal and conservative Californians believe the time may now be ripe for another attempt at the ballot box. Roger Magyar, a Republican Party activist and state official during Reagan's administration in Sacramento, and Leroy Chatfield, a former United Farm Workers organizer and the manager of Jerry Brown's 1976 presidential campaign, have put together an organization called Parents Choose Quality Education. Their voucher plan has won the endorsement of Milton Friedman, and they hope to win sufficient signatures for placement on the June '84 primary ballot.

There has been a dramatic increase in popular support for vouchers in the last few years. Indeed, 1983 was the first year in which a majority of Americans in a national survey expressed support for education vouchers. A Gallup Poll conducted last June indicated that 51 percent of Americans would like to see a voucher system adopted in this country; 38 percent would not, and 11 percent had no opinion. The favorable responses were up from 43 percent in 1981 and 38 percent in 1971.

The youngest group surveyed—people 18-29 years old—were most in favor of vouchers (60 percent for, 29 percent against, 11 percent no opinion). And blacks at the grassroots level are even stronger in their support (64 percent for, 23 percent against, 13 percent no opinion). Yet many veteran civil rights leaders are adamantly hostile, because a variant of vouchers was briefly used in the South by local school boards and state governments during the 1950s to try to stave off school integration.

Likewise, despite the strong support among Catholics for vouchers (63 percent for, 29 percent against, 8 percent no opinion)—not to mention the fact that some 3 million youngsters are attending Catholic schools in 1983-84—the US Catholic Conference has never taken a public stand for vouchers. Individual priests and bishops have supported the idea, but they have no solid institutional backing.

Roger Magyar told REASON that in California, church officials are apprehensive that a voucher system might exclude parochial schools, either from the beginning or later at the behest of a court ruling. Meanwhile, the American Civil Liberties Union is against vouchers for the opposite reason: it's worried that a voucher system would *include* parochial schools. Burt Neuborne, legal director of the ACLU, told REASON that the organization is opposed to vouchers on Establishment Clause grounds (the constitutional provision that "Congress shall make no law respecting an establishment of religion").

The irony here is that civil libertarians should be a natural constituency for vouchers. After all, government-run schools routinely trample on the civil liberties of families who disagree with the way their children are educated.

Clearly, the popular support for vouchers in this country has survived and prospered without nurturing by the political establishment. One can only conclude that parents' alienation from the current state monopoly in education is very strong indeed. So while economists propose and teachers unions dispose, the mass of parents out there may well come to consider education vouchers as natural as generations of small-town Vermonters have found them. ◻

John McClaughry, formerly a senior policy advisor in the Reagan White House, went home to Vermont in 1982, where he runs the Institute for Liberty and Community "way back in the woods." This article is a project of the Reason Foundation Investigative Journalism Fund.

BUYING OUT OF SOCIAL SECURITY

Congress saved Social Security? Don't bet on it. We need a different kind of solution.

BY LOREN E. LOMASKY

Come 12:01 on the morning of January 1, the Social Security tapeworm will celebrate the New Year by curling up for a delicious new feast, compliments of America's wage earners. Because of legislation passed in April 1983, ostensibly designed to stave off the bankruptcy of Social Security, the ravenous system will take an even larger bite out of paychecks than before.

For those unfortunates already paying into the system, the Social Security tax will go up from 6.7 percent to 7 percent and the maximum annual

ILLUSTRATION BY TOM CARDAMONE

contribution (calculated for a wage base of $37,500) will rise from $2,392 to $2,625. These are only the first squiggles in a long-term upward spiral. By 1990, the Social Security tax rate is scheduled to rise to 7.65 percent and the maximum contribution to $4,200.

New Year's Day will also mark the addition of new dishes for the system's ever-growing appetite. Most notably, the paychecks of newly hired federal workers and of all employees of nonprofit organizations will be subject to the same tax—and at the same rate—as their fellow workers.

It is instructive to recall that the 1983 legislation, the tapeworm's new meal ticket, came about as a result of the Social Security Crisis. Those with long memories will recall that in early 1983, Social Security pushed nuclear weapons to a distant second in the hierarchy of crises, and that old chestnut the Energy Crisis was nowhere to be seen.

Normally when a crisis is announced, the single best policy that Washington could (but usually does not) adopt is doing absolutely nothing. What these crises really signify is that some entrenched bureaucracy is eager for a raid on the Treasury. If it gets what it wants, things will surely get no better and will probably get worse. If the worry is why Johnny can't read, the response is to toss federal dollars into education, create a new cabinet-level agency, and watch SAT scores plummet to the level of a utility infielder's batting average. If OPEC connives to raise the price of oil, the government declares an energy crisis, baptizes yet *another* cabinet post, and produces lines at gas pumps that would gladden the stern heart of an ayatollah.

Unfortunately, when the crisis is itself the direct fruit of misguided governmental policy, the usually sound advice doesn't always apply. Such is the case with Social Security. A string of presidents and congresses have shown their compassion for America's aged (and, incidentally, for their own incumbency) by creating an actuarially unfunded debt of $6 trillion, give or take a trillion. Pundits now learnedly debate whether the system will go belly-up before 1990 or expire in a sea of red ink early in the 21st century. If you believe the former, you are officially dubbed a "pessimist," if the latter, an "optimist."

The response to this particular crisis observed all the traditions. First the president's National Commission on Social Security Reform spoke, and then a resounding echo was heard in the Congress. The results were entirely predictable. Your newly revised version of Social Security features not only higher payroll taxes but also a tap on the Treasury's general revenues, the inclusion of millions of formerly exempt warm bodies, a brief pause in cost-of-living adjustments, and some taxation of retirement benefits. Chances are now excellent that no Social Security check will bounce anytime in the next decade.

Polite folk and those who have taken to heart John Maynard Keynes's dictum, "In the long run we are all dead," will not inquire further. However, the rest of us are advised to refrain from applause just yet. In his State of the Union address last year, President Reagan warmly applauded the bipartisan spirit that generated this pact, reserving special praise for the Speaker of the House, not hitherto noteworthy as a recipient of Reagan's plaudits. Such comradely benedictions indicate either that a new spirit of statesmanlike fellowship roosts on Capitol Hill or that taxpayers should grab for their wallets.

The package is—pick one—a delusion or a disaster. The tax increases called for will slow or halt recovery. Solvency in the near term requires that optimistic economic forecasts come true—not a good bet on the past record. Nothing has been done to address the dilemma for Social Security early in the next century, when the postwar baby boom generation retires with few wage earners available to support it. Indeed, the legislation has exacerbated this problem. By dragooning government employees into the system, funds will be made available in the near term, but at the cost of many more checks to mail out a few decades hence. Most important, "reform" measures have done nothing whatsoever actually to reform the system—Social Security will continue to be a ripe target for political gamesmanship. It is a near certainty that periodic crises will remain with us. What then should be done?

Will the system go belly-up before 1990 or expire in a sea of red ink early in the 21st century?

In fact, there is no quick fix to the Social Security dilemma, else I would have announced it two paragraphs back. Raising the tax rate promises to produce supply-side miseries that will multiply unemployment; but to cut promised benefits to the elderly would be to default on the compact between government and citizen. Nor, in case one has failed to notice, does there exist a healthy Treasury surplus from which funds can be obtained.

Perhaps there is no very attractive solution to the Social Security mess. Then we must look to the least bad response that can be designed. The following four criteria ought to be applied to proposed strategies as a test of their political, economic, and moral soundness:

(1) Whatever plan is adopted must not leave economic carnage in its wake. Part of the reason for Social Security's current parlous state is the fact that our economy has been in the doldrums for a decade. Prolonging or increasing economic misery is no way to secure the financial foundations of Social Security or of any other government program.

(2) The fact that past congresses and presidents have lavishly promised benefits through Social Security which they have failed to fund adequately may amount to malfeasance of duty. It does not follow, though, that ill-made promises are null and void. Those now past or approaching their 65th birthday have planned for retirement with the expectation that Social Security will be there to meet a large chunk of their needs. Those expectations carry moral weight even if they rest on political legerdemain. It would be unjust to violate them at this late date.

(3) Those Americans who had the good luck to be born between 1880 and 1920 have enjoyed and will continue to enjoy benefits from the retirement provisions of the Social Security system far in excess of their contributions to it—perhaps averaging five times greater than what an actuarially sober pension plan would have afforded. To put it another way, Social Security is 20 percent pension, 80 percent Ponzi scheme. That means that younger participants must inevitably be net losers. It is too late to take back any but a negligible amount of benefits from pre-1920 generations. What can be done, however, is to spread the losses as evenly and fairly as is now possible among the various age groups. Any proposal that pretends to offer a way out that hurts no one must be viewed with a jaundiced eye.

(4) Whatever remedy is offered must realistically address the

problems that actually exist and, above all, be immune to recurrent financial hemorrhages a few years down the road. Congresses and presidents have repeatedly produced legislation advertised as "solving" the problems of Social Security; as recently as 1978, President Carter announced that he had signed a bill guaranteeing the soundness of the system through 2030. The gloomy record of repeated past failures should make it clear that superficial tinkering with tax and benefit schedules can, at best, temporarily postpone the day of reckoning.

Now for the salvage operation. Paradoxically, one factor that makes rescue more plausible now than ever before is the American public's awareness of the quagmire into which Social Security has fallen. In a national survey, an astounding 84 percent of those between the ages of 18 and 44 said that they do not believe that benefits will still be available when they retire. They recognize that they are at the tail end of a chain-letter boondoggle that is about to collapse. Presumably, then, they are willing to cut their losses rather than hold out for a dubious jackpot, the prospect of which they see steadily receding.

Those 45 and younger can count on at least 20 working years remaining during which they are able to accumulate a retirement nest egg. Accordingly, I propose that those who are 45 years old be offered the option of not paying any further Social Security payroll taxes. If they choose this, they would, of course, no longer be eligible upon retirement to receive benefits. But the money they would save on tax payments would then be available to them for investment in private IRAs (individual retirement accounts) or Keogh-plan accounts.

Probably Congress would not allow people to gamble on their longevity or continued ability and willingness to work after age 65 and thus would insist on making mandatory the purchase of some minimum level of pension benefits. Strict libertarians would demur, but a legal requirement of *private* retirement investment is still a giant step toward voluntarism.

Those who elect to continue to pay Social Security taxes could still do so, but it would be stipulated that their retirement payments would be actuarially determined according to the present value of their lifetime tax payments, not by the largesse of Ronald Reagan and Tip O'Neill's 21st-century successors. This provision should satisfy the legitimate claims of every working 45-year-old: those who view Social Security as a sinking ship would be free to abandon it; those who are more optimistic would be guaranteed a return based on every dollar put in.

For those between the ages of 16 and 45, payroll taxes would still be collected, but on a sliding scale ranging from 100 percent of the current rate for those under age 25 down to zero once the 45th birthday is reached. That would be their cost of "buying out" of the system, and it is appropriate that they carry their fair share of the burden. Again, they would not be *required* to leave the Social Security system at age 45, but would be *permitted* to do so if they wished. The difference between the tax they would be required to pay and the current payroll tax could be directed either to a private pension plan or to a government-operated one, the latter perhaps still called "Social Security." Given the reality of government's inefficiency in almost every area it touches, one might suspect that most people would choose to take their chances in the private sector. That, however, would be up to them. Galbraithian liberals could display their allegiance to New Deal principles by continuing to send their dollars to Washington.

It would be unjust to require that all sacrifices be made by younger people. Those above 45 but not yet retired would be given two options. They could drop out of the system, in which case upon reaching age 65 they would receive from Social Security a pension based on the then-current value of the money they contributed. Or, they could stay with the system at its current benefit level but be required to make payments larger than the current payroll rate dictates in order to make the benefit levels commensurate with the system's revenues.

Finally, those now retired would not have benefits diminished. Instead, amounts would be frozen for a 3-year period. This would offset previous overly generous cost-of-living adjustments. How much this would affect pensioners would depend on the rate of inflation during this period. If inflation were kept very low, pensioners' living standards would suffer hardly at all. A useful side benefit of this reform is that, in one fell swoop, it would create a politically powerful constituency adamantly opposed to inflationary policies. Could even Teddy Kennedy and Lowell Weicker resist its demands for fiscal sobriety?

After the 3-year freeze, benefits would be adjusted, but this time by reference to the average wage level and not the Consumer Price Index. The old deserve both our respect and their fair share of the growth of real income; they are not, however, entitled to be the one group of the population entirely shielded from the baleful effects of inflation.

Any proposal that pretends to offer a way out that hurts no one must be viewed with a jaundiced eye.

Should the standard retirement age be kept at 65 or raised? One beauty of the proposal outlined above is that no answer need be given—that is, no one answer would necessarily emanate from the hallowed precincts of the Social Security Administration. If pensions were fully funded, each individual could choose his own retirement date. Those who would elect to retire early (say, at age 55, which is not currently allowed under Social Security) would receive relatively small monthly payments. Those who chose to work until a ripe old age could receive, upon retirement, very substantial payments. Washington could get entirely out of the game of fixing a mandatory retirement age.

Some will object that this proposal is unfair to the young—those under age 45 would be compelled to pay into a system from which they could not subsequently receive benefits (unless they elected to fund their retirement through the government program). On what ethical grounds could they be *compelled* to sacrifice for the sake of older, more fortunate age groups?

It is true that the young would be net losers—losers, that is, relative to a world in which Social Security had never existed and thus a world in which no one had to fund a pay-as-you-go transfer scheme. Alas, that world ceased to exist during the New Deal. The reality that must now be confronted is that the government has vast unfunded retirement liabilities, and only

two alternatives are available—defaulting on those liabilities or somehow apportioning their cost. My proposal places some of that cost on the young—and some on every other age group.

In fact, compared to their treatment by the present system, the young would be the *major winners*. For if Social Security were finally to expire early in the next century, those who are now young would lose a lifetime of taxes pumped into the floundering system. By then, Claude Pepper and his cronies will be in that happy realm in which fiscal mismanagement is unfelt. Better an opportunity for the young to buy out now than suffer truly disastrous consequences later.

Were it the case that Social Security could be terminated without cost to anyone, then my proposal to spread those costs equitably would be superfluous. But no such cost-free alternative is available, for the simple reason that in every transfer system in which some are gainers, others must be losers. If each of seven poker players claimed to have come out of the night's action a winner, you would suspect their veracity. For exactly the same reason, you ought to question the logic of any plan for phasing out Social Security that purports to be painless.

Congressman Ron Paul (R-Tex.) has proposed a scheme with such claims. His suggestions for funding benefits in the close-out period range from the fanciful (minting and selling American Gold Eagle coins to the public) to the sober (using the savings that would accrue with the elimination of military and economic foreign expenditures). Suppose that such devices would suffice to pay extant claims. Would this place any less of a real burden on taxpayers than the proposals I have outlined? The answer is clearly no.

Let us grant, for the sake of argument, that foreign expenditures ought to be terminated. This should provide relief to taxpayers no longer coerced into paying for foreign involvements. That is all to the good. But Paul does *not* propose leaving that money in the hands of its rightful possessors; instead, he would divert it to Social Security.

Note that this is *real money* that has been extracted indiscriminately from all taxpayers. It is plainly dishonest to pretend that such tax money is "found" revenue, a kind of manna from heaven. Moreover, it is unfair to rely on taxpayers to save Social Security. Although everyone would be burdened by this strategy, high-income earners and the young would suffer most—the former, because they have higher tax rates; the latter, because their taxpaying would last the longest.

These considerations apply to the other revenue devices Paul proposes. If one believes that the US tax code is so scrupulously fair that no attempt to distribute the Social Security burden can improve on it, then one ought to favor his proposal. Otherwise, one should admit that we can do better. The big "advantage" of the Paul proposal over my proposal is that his attempts to hide the true cost borne by different parties, while mine makes such information public.

The observant reader will have noted that the immediate effect of adopting my proposal would be a very slight decrease in Social Security benefits paid out and a large decrease in receipts. Since the retirement fund is already running a deficit, it may appear that the otherwise laudable features of the proposal are obliterated by that imbalance.

There is an answer to this objection. My proposal would result in a deficit on the order of $50 billion per year over the next two decades. This could be made up largely by selling off the federal government's vast land holdings, including subsurface rights. (National parks could be exempted.)

The value of the national domain is hard to calculate. Several current estimates are near the $500-billion figure. They are biased downward, however, by the fact that governmental restrictions on use of this land cause great inefficiency in its exploitation, as well as the fact that this land has not been carefully surveyed for potential commercial opportunities. Thus, its market value may actually be closer to $1 trillion. If it were sold off over a period of 10 years, proceeds could be diverted to funding Social Security.

Once the land is in private hands, it would be subject to property tax, and profitable commercial ventures would generate income also subject to taxation. These taxes could be applied to the payment of retirement benefits until Social Security is once again a solvent concern. Subsequently, disgorged property would be taxable by local jurisdictions, another constituency that should welcome this proposal.

Of course, selling federal land would impose burdens on citizens. You would lose "your claim" to a share of the national domain. It is unlikely, though, that this not-very-liquid asset ever figured prominently in your estimation of your own net worth. Environmentalists would surely howl. Against them, an effective rhetorical retort might be, "Which do you value more—landscapes, or your parents and grandparents?" If this does not pacify the Sierra Club, perhaps it will be mollified by the thought that every tree sold off is a tree that the politically buffeted federal government can't touch. Others, of course, regard the privatization of the national domain as a positive benefit, as desirable in its way as the restoration of solvency to Social Security.

It may be feared that the money spent by private interests in buying up the national domain would diminish the already low supply of capital available for investment. If investment in plant and equipment ground to a halt while land was being auctioned off, the economic consequences would indeed be catastrophic.

But what this objection overlooks is that my proposal calls for a shift to a regime of fully funded pension programs. Workers who put their earnings into such pension accounts would thereby be supplying capital that the United States needs to achieve real economic growth once again. On balance, the two would roughly cancel out during the transition period. And following the complete privatization of the national domain, pension funds would provide an enormous infusion of capital.

Finally, some will complain that this proposal "saves" Social Security by destroying it. The program that would remain in government hands would not be mandatory, would not feature near-universal participation, and would not be able to transfer huge sums between generations.

All that is true, but it misses the point. My proposal cannot destroy Social Security, because Social Security has *already been destroyed* by decades of political profligacy. Congresses have shown themselves thoroughly unable to restrain themselves from dangling goodies before voters, goodies to be paid for later.

Proponents of a mandatory government retirement program have often employed the paternalistic argument that individuals cannot be trusted to provide for their own retirement; the all-wise overseers in Washington must do it for them. But if *you* don't save today, then it's *you* who will be impoverished 20 or 40 years hence. A congressman who votes today to increase benefits, however, will be safely out of office 20 years from now—and probably enjoying a fat congressional pension. Ironically, it is *government* that cannot be trusted to provide for individuals' retirement. ◻

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TAKING IT ON THE ROAD

They've got their transportation deregulation act together in Arizona, but some carriers want to close down the show.

BY JOHN SEMMENS

"We've tried deregulation, and it doesn't work," proclaimed Bill Arnett, owner of Yellow Cab of Phoenix. He was speaking to Arizona's House Transportation Committee in early 1983—before Arizona's deregulation of intrastate motor carriers had been in effect even for a year.

Arnett's firm conclusion, often repeated by deregulation critics, was supported by no specific evidence of any kind. Though deregulation opponents often refer vaguely to "unreasonable" taxicab fares, there are no data giving flesh to this claim. Insubstantial as the charge of unreasonable fares is, this alleged consequence of deregulation is mild compared to the predereguation forecasts of rising incidences of rape and murder that would accompany the abandonment of regulation.

Impartial observers might view this condemnation of deregulation as an unduly hasty conclusion. After all, regulation had been "tried" for over 60 years. Since 1921, when Arizona's regulatory body, the Corporation Commission, ordered an operator of an unscheduled limousine-type service to charge no less than 140 percent of the fares charged by scheduled carriers—and a court upheld the order—Arizona had suffered under the most restrictive transportation control in the nation.

Despite the state constitution's explicit language pledging that monopolies "shall never be allowed in this State," regulators coddled the motor carrier industry with a rigidly controlled system that guaranteed virtual monopoly positions for approved carriers. Arizona's regulatory regime was comprehensive:

PHOTOGRAPH BY BOHAN HRYNEWYCH

all motor vehicles transporting freight or passengers for compensation were subject to regulation. The fundamental issue, in any case, is the same, regardless of the type of service provided—namely, should people be free to exercise choice or not? The rationale for enforcing a pervasive monopoly system was to "prevent unnecessary duplication of service." This the state did with stolid dedication, even to the point of absurdity.

A 1966 state supreme court decision demonstrates the absurdity of Arizona's regulatory scheme. The court case had its origin in 1948, when a firm proposed to establish a door-to-door refrigerated-van service to various points in Arizona. Even though no licensed carriers provided such a service, a number of them protested the new firm's application. Under Arizona law, carriers holding "territorial" operating rights had to be given the opportunity to provide any new service in their "territory."

The Corporation Commission, charged with the responsibility of enforcing the regulatory system, gave existing licensed carriers 60 days to initiate a refrigerated-van service. Then, after 60 days, the new firm's application was dismissed—on the grounds that the proposed refrigerated-van service was now being provided by existing operators! The would-be new firm, its marketing innovation expropriated, was sent packing.

By 1953, the carriers with territorial monopolies had discontinued refrigerated-van service. So the same firm that had originally proposed this type of service made a new application for operating authority. This time, the Corporation Commission, observing the lapse of refrigerated-van service, awarded an operating certificate. The existing licensed carriers sued, and after lengthy litigation the Arizona Supreme Court ruled in their favor in 1966.

Before new authority could be awarded under Arizona regulations, the court ruled, it had to be shown that existing carriers had refused to provide service, but their failure to do so was not proof of their *refusal* to serve. Before a new firm could be awarded operating rights, the court ruled, existing carriers had to be given another opportunity to provide the service. Thus, no matter how many times an existing carrier might allow a specific service to lapse, no matter how much dormant authority might exist, no new firm could be permitted into the market without the acquiescence of the existing carriers.

The inhibiting effects of this regulatory scheme are not difficult to perceive. Any person wishing to provide a new service was required to present, in detail, the whole proposed operation. The new applicant had to show a need for the service, thereby disclosing a potential market. Ability to serve had to be shown, thereby illustrating how this market might be served. After going to some expense to expose the profit potential of some new service, the new applicant would have no protection against the expropriation of his market idea and operating plan.

Given this absurd regulatory scheme, it is not surprising that poor motor carrier service was cited as a negative factor in a 1972 Batelle Memorial Institute report on Arizona's economic growth potential. And since state regulations applied to all motor carriers, including taxis, it is not surprising that in qualitative measures of taxi service, Phoenix came in dead last among a survey of 30 major metropolitan areas conducted in the early '70s.

At the Phoenix International Airport, the scene of alleged taxi-fare "rip-offs," signs clearly inform travelers that rates for the deregulated taxis, limousines, and buses may vary.

In a more perfect world, a mere showing of the negative results of a government-mandated regulatory program might be enough to cause its demise. In the real world, though, such a showing is not enough. Indeed, in early 1983 an Ohio court ruling—reaffirming the state's authority to regulate prices of alcoholic beverages—stated that if a mere proof of negative outcome were sufficient to overturn government regulations, the government wouldn't be allowed to regulate *any* economic activity.

Costly, harmful government rules persist as they do because a small group of persons reaps some benefit, and although the benefit may be dwarfed by the costs, the costs are broadly dispersed. For example, before the interstate trucking industry had begun to be deregulated—in 1980—the total cost of the negative impacts of regulation outweighed the total benefits to the truckers by a 30-to-1 ratio (see my "Regulation of the Truckers, by the Truckers, for the Truckers," REASON, March 1979). At the same time, the benefit per regulated trucker outweighed the cost per victimized consumer by at least 400 to 1.

The beneficiaries of motor carrier regulation, though a minority, have powerful financial incentives to promote and preserve harmful government controls, and overcoming the influence of this minority requires persistent effort. For example, for several years prior to enactment of Arizona's motor carrier deregulation, Prof. Jonathan Rose, of the Arizona State University's law school, made almost annual appearances at the state legislature to testify in favor of deregulation. Staff employees at the Corporation Commission and the Arizona Department of Transportation conducted research and collected data for nearly two years before the deregulation bill passed. But meanwhile, various private-interest coalitions were bringing persuasive influence to bear on the legislative process, trying to block deregulation. Thus, though a deregulation bill was passed in 1979, and the law was to go into effect only if the voters reaffirmed it by referendum—which they did by a 2-to-1 margin—regulation defenders were able to postpone the legislation's effective date to July 1, 1982.

After years of struggle, Arizona's motor carriers were finally deregulated. And though opponents of deregulation vociferously predicted that chaos would ensue, no evidence of chaos has come to light. The minor disturbances that *have*

arisen in Arizona's trucking industry have been protests over increased state and federal taxes on heavy vehicles. (At the same time that deregulation was enacted, Arizona implemented a new weight-distance tax aimed at collecting a larger share of highway-user taxes from heavy trucks. And in December 1982, Congress voted to raise the federal heavy-vehicle use tax, in phases, from $240 to $1,900 by January 1984). The unfortunate concurrent implementation of both deregulation and higher truck taxes in Arizona confounds attempts to evaluate the effects of the new market regime in motor carriage.

But there is no mystery surrounding the way regulatory restrictions generally affect motor carrier service and charges. So certain results of the removal of regulation can be predicted. In short, we would expect the quantity of service to increase and freight shipping charges to decrease. On the other hand, the simultaneous tax increase would put upward pressure on shipping charges. Moreover, we would expect the increased operating costs occasioned by the tax hike to restrain service expansion. Consequently, we could imagine that rates might go up and service decline, all because of the tax increase, but with deregulation taking the blame.

Yet the issue of deregulation fundamentally is one of freedom—entrepreneurs and consumers should be free of government interference in their voluntary economic activities. Still, it is fortunate for those who prize economic liberty that the overall effects of Arizona's motor carrier deregulation have been favorable. Indeed, in a survey conducted in November 1982, and published in January 1983, for the Arizona Department of Transporation, Profs. Richard Beilock and James Freeman, respectively of the universities of Florida and Kentucky, found that deregulation seemed to be producing the expected beneficial results. To carry out the survey, they sent a questionnaire to 160 carriers and 787 shippers and receivers in Arizona. Seventy-three carriers and 231 shippers and receivers returned the questionnaires.

No doubt, a survey of people's perceptions of the effects of deregulation will disappoint some people. Those quantitatively inclined would be more impressed by an index of freight charges or a measure of service capacity. But there are two key reasons for rejecting such an approach. First, assuming that a valid index could be compiled, there would be no way to segregate the various possible causes of changes in the index. Asking instead for an informed judgment on the part of users and providers helps to deal with the causation question.

Second, values are subjective. The valid measure of consumers' benefit is whether they are more or less satisfied with the value received as *they* themselves perceive it. Since an individual consumer purchases a complex mixture of services at varying prices, an aggregate statistic purporting to show an average price may be more misleading than we like to think: the trade-off between price and quality can be very subtle. It is by no means obvious, then, that an economist's classification and measurement of various grades of service at various prices is superior to consumers' own perceptions as a gauge of consumer benefit.

Taxis waiting at the Phoenix airport's cab stand have their rates posted on their doors, and signs urge taxi users to determine fares before getting into cabs.

Of all the various forecasts of the effects of deregulation, Beilock and Freeman's survey most outstandingly confirms those concerning competition. According to the survey, taken nearly six months after the effective date of intrastate deregulation, overwhelming majorities among users and providers of trucking service perceived greater competition following decontrol. A ratio of 12 to 1 users thought competition had increased, and among providers, the ratio was nearly 8 to 1.

It could hardly be otherwise. Carriers have gone from a system in which only government-authorized operators could provide service, to one in which there are no restrictions on service or prices—any carrier may serve any shipper anywhere in the state, and all rates are left completely to the market.

Increased competition has manifested itself in new service offerings and in various rate discounts, practices unheard-of in the prior, regulated regime. Almost half—47 percent—of the surveyed users of trucking service reported that new carriers had solicited them with proposals to provide service, and 45 percent reported offers of rate discounts for selected shipments.

The effects of increased competition, however, have not been uniform. As would be expected, some areas of the market have experienced a greater response to the expanded freedoms. Thus, while nearly half of the surveyed shippers reported some discount offers, about two-thirds hadn't seen any significant overall change in rates. But among shippers who *did* perceive a general change in basic rates, those reporting a *decline* outnumbered, by more than 2 to 1, those reporting an increase.

It is in the assessment of deregulation's effect on rates that the confounding influences of increased truck taxes may be wreaking its havoc. Nearly two-thirds of the shippers and receivers responding to Beilock and Freeman's survey felt that the higher truck taxes had made freight charges higher than they would have been otherwise. Whether these higher taxes nullified any possible rate declines due to increased competition cannot be determined. But it is significant nonetheless that despite this tax hike, rates still appear to be somewhat lower on average.

Opponents of deregulation might concede that customers in the busy metropolitan areas would benefit from removal of controls. But people in small towns, these critics are wont to warn, would suffer. Government controls aid in the establishment of cross-subsidies (excess profits in urban markets with which carriers could subsidize unprofitable rural service). From an equity standpoint, the enforcement of monopoly profits from excess charges on urban shippers is reprehensible—why should urban users of motor carrier service subsidize rural

PHOTOGRAPHS BY JOHN SEMMENS

Alaska, Colorado: Grassroots Reform

The fresh breezes of transportation deregulation may soon be felt beyond the borders of Arizona. In Colorado and Alaska, pro-free-market groups are turning to the ballot initiative to put strong deregulation measures to a vote.

In Colorado, the effort is being led by a group called Coloradans for Free Enterprise (CFE). The state's constitution stipulates that public utilities are subject to state regulation, and common carriers have always been regulated as such. The CFE strategy is to work for a constitutional amendment specifying that motor-vehicle carriers are not public utilities and hence are not subject to regulation. This would have the effect of lifting the hand of the state from package delivery, intercity buses, taxi and jitney services, and household-goods movers.

According to Paul Grant of the CFE, the group is now working to meet the legal requirements for a petition drive that would get the measure on the ballot next November. The petition campaign itself—with a goal of 47,000 signatures—is scheduled to be launched in February, but the issue has already been well publicized throughout the state. Grant has given several speeches on deregulation and was in a debate last fall with Denver University law professor Paul Dempsey, a federal official under Carter and a nationally known supporter of regulation.

In the statehouse, several Republicans have voiced opposition to the deregulation initiative, but it has won the support of a number of Democratic liberals. "The Democrats see the current regulation as protecting special interests and anti-consumer," explains Grant. "And they're right."

Deregulation has also garnered the support of "victims of the Public Utilities Commission," Grant told REASON. An example is Jack Rivera of Senior Cab. Rivera hoped to start a taxi service for senior citizens, providing three rides a week anywhere in the Denver metropolitan area, at any time, in exchange for monthly "dues" of $30. In case of medical emergencies, the rides would be in oxygen-equipped vans driven by trained medical technicians.

In spite of popular enthusiasm for the idea, the Public Utilities Commission demurred. The agency claimed it would be "unfair" for Senior Cab to charge a flat monthly rate rather than a mileage-based rate. But with a small-scale political lobbying effort, Rivera was eventually successful in getting the PUC decision overruled. He is one of the few people to have taken on the PUC and won, but, even with his own problem solved, it was not hard to enlist him as a supporter of the deregulation initiative.

In Alaska, the deregulation forces are setting their sights high, aiming for complete abolition of the Alaska Transportation Commission (ATC) and repeal of virtually all the regulations the commission now administers. The only state requirements to be left intact would be that private firms show "financial responsibility" (by obtaining insurance or posting bond) and meet existing requirements concerning safety. Administration of both requirements would be transferred to other agencies.

Dick Randolph, chairman of Alaskans for a Competitive Economy and leader of the deregulation drive, told REASON that Alaska now "probably has the most heavily regulated intrastate transportation in the country." For example, the Transportation Commission rigidly controls firms' entry to and exit from the air and surface transportation market and has no compunction about denying applicants' petitions. And because of Alaska's size, transportation is an especially important part of the state economy.

Like their counterparts in Colorado, the Alaskans hope to qualify for the November 1984 ballot. They need a minimum of 20,000 qualified signatures by January 9 but are hoping to gather at least 27,000. The campaign to gather signatures began in earnest in September.

Randolph, a former Libertarian state legislator and a veteran of Alaska's "Tundra Rebellion" and income-tax repeal initiatives, noted that political battle lines will probably not be drawn until after the initiative qualifies for the ballot. He expects the strongest opposition to come from the Teamsters Union and from transportation firms that have benefited from ATC protection from competition.

At the same time, Randolph seems confident that a strong base of consumer support for deregulation exists. "In Alaska," he says, "people get on the bandwagon after the signatures are gathered."

—P. G.

users? Nonetheless, this cross-subsidy scheme was actually touted as a rationale for opposing deregulation.

As it turns out, Arizona's rural trucking-service users perceive almost as much benefit from deregulation as their urban counterparts. More than 60 percent of the rural shippers and receivers surveyed observed increased competition for freight. Almost 40 percent received offers of new service, and more than a third have been offered discounts from regular shipping rates. While more than 60 percent saw either no change or were uncertain of whether there had been a change in overall rates, a slight plurality of those who did see a change thought rates had come down.

Unsurprisingly, the prederegulation forecasts of the regulated carriers were not borne out. Far from being abandoned, small towns in Arizona have shared in the general beneficial effects of deregulation. More service seems to be available, sometimes at discount prices. Rates, instead of going through the roof, appear to be, if anything, somewhat *lower* than under the regulated system—again, in spite of a tax increase.

Well, say deregulation opponents, maybe the small towns do all right, but surely the small shippers must be hurting—without government controls, the big shippers can throw their weight around and get the best deals while the little guy suffers. Once again, however, the data show that the market provides better protection for everyone, including the little guy. While Beilock and Freeman's survey found that more big shippers perceived improvements under deregulation, many small shippers also gained from the removal of controls. Almost 40 percent received offers of new service, and more than a third were offered discounts. By a ratio of 10 to 1, those who saw a change in competition thought competition had increased. And of those who perceived an overall trend in rate changes under deregulation, more than twice as many saw rates declining as saw them rising.

As I noted earlier, motor carriers, too, perceived an increase in competition, and more than a third of those surveyed by Beilock and Freeman have changed the way in which they establish freight charges. Their favored new methods are (1) meeting the competition and (2) set-

(Continued on p. 49)

In Defense of the Corporate Coup

Why mergers make the market work better

BY HENRY G. MANNE

Du Pont pays $7.5 billion to buy up Conoco. Santa Fe Industries and Southern Pacific agree to merge in a $5.2-billion deal, creating the third largest railroad in the country. Allied acquires Bendix for $2.3 billion in a celebrated takeover battle started when Bendix tries to absorb Martin Marietta. How could such high-priced shuffling of corporate assets possibly benefit the economy?

The popular wisdom is that it doesn't and can't. Harvard professor Robert Reich, darling of the neo-liberals, is typical of the most recent anti-merger sentiment. In THE NEXT AMERICAN

ILLUSTRATION BY MICHAEL BEICKEL

Frontier, his apologia for a government industrial policy published last spring, Reich put corporate mergers at the top of his list of sins of "paper entrepreneurialism." Soon *Time* magazine was characterizing corporate takeover battles as "paper chases."

But if Reich managed to coin a catchy label, he is not alone in his view that the business mergers that have been making headlines don't make much economic sense. Here are already-huge corporations apparently diverting their firms' resources from production or from their own stockholders. Often, in "hostile takeovers," the managers of the "target" firms don't want their companies to be acquired. The "raiding" corporations seek to gain control anyway via tender offers—using public solicitations to buy stocks directly from the target firms' shareholders, at high premiums over the stocks' market value. Thus the parries, thrusts, and billion-dollar deals that can seem like a waste of time and money.

Why should antitrust laws be used to block mergers that the market, by the existence of willing buyers and sellers, shows to be desirable?

"I think it is time for the Congress to send a clear signal to corporate America that we will no longer tolerate unrestrained warfare between top management for control of corporate assets," declared Rep. Peter Rodino (D-N.J.) last summer, when he introduced legislation to restrict large mergers. The proposed measure would ban any large mergers not deemed to be "in the public interest" by the Justice Department and the Federal Trade Commission. The two agencies would be enjoined to judge a merger's effect not only on competition (that, they've *always* been empowered and eager to do) but on employees and the "effective management of corporate assets." Whether or not the legislation passes—it seems unlikely at this time—it embodies widely held sentiments.

Meanwhile, the Securities and Exchange Commission (SEC), the government's main arm of stock-market regulation, is carrying on a review of tender-offer policy. Tender offers are used in only a small percentage of mergers; in 1982, for example, there were 2,400 mergers, of which 94—only 3.9 percent—involved tender offers. But these are the ones that can make news in the mass media, and in the wake of the Bendix-Martin Marietta battle in late 1982, the SEC initiated a study of its regulation of corporate takeovers, with a view to better protecting stockholders' interests.

Up till now, the government's primary weapon against mergers has been the antitrust laws. Mergers, particularly among firms in the same industry, have often been deemed among the least defensible kinds of behavior under US antitrust laws—right up there with price fixing.

Thus we find the Federal Trade Commission (FTC) voting unanimously in 1982 to stop Gulf Oil from buying Cities Service, claiming that the proposed merger could jeopardize competition. The FTC's action succeeded, as Gulf withdrew the offer, citing antitrust obstacles, although other factors may have been involved as well.

The FTC also challenged the acquisition of two hospital chains by the Hospital Corporation of America, because its share of the acute-care market in a 13-county area around Chattanooga, Tennessee, would rise from 16-17 percent to 30-32 percent. Further evidence of the supposed threat to competition was the estimate that the company's share of the market for inpatient-psychiatric services in the same geographic area would rise from about 7 percent to about 38 percent.

The antitrust laws also played a major role in stopping Mobil's attempt in 1981 to take over Conoco and then Marathon. Du Pont won the contest for Conoco, but its ability to acquire it at $98 a share, compared to Mobil's offer of $120, was helped by threats from the FTC and the Justice Department to go to court against Mobil if it won. Investors were properly concerned that if they accepted Mobil's offer, the deal would later be nullified.

Later, Mobil failed to acquire Marathon even though it offered up to $126 for stock that had been selling at $64. Marathon executives secured an injunction against Mobil under the antitrust laws, and the FTC proceeded to file suit in opposition to the takeover. Marathon executives were thus able to fend off Mobil in favor of a "friendly takeover" by US Steel.

Why should the government, and sometimes incumbent management, be using the antitrust laws to block mergers that the market, by the existence of willing buyers and sellers, demonstrates to be desirable? The long-standing rationale is a fear of monopolization; consumers are to be protected from high prices by preventing industry concentration via merger. Under new proposals, the government would gain additional weapons, ostensibly needed to protect shareholders and the public interest. Unfortunately, all this ignores significant new learning in economics—the discovery of how capital markets, unlike government regulations, actually serve the public and provide protection for consumers and shareholders.

Briefly, the apparatus works like this: The stock market accurately measures and reflects in the stock price the relative quality of each company's management. If for any reason a company is receiving lower-quality management than someone else would be willing to provide, the company's stock will be priced lower accordingly. This lower price will attract the interest of competing managers who see an opportunity to give better management to the company. They will want to purchase enough of the company's stock, for which they will have to offer a premium over its low market price, to acquire managerial control. By better management, they hope to realize a gain on the shares purchased.

Takeovers assure significant competition for managers' positions, thus spurring them to act in the interest of shareholders.

In this light, modern economic scholarship has shown the traditional view of mergers—as a threat to the competitive economy—to be a highly simplistic and even perverse view of things. For while there is a possibility of market power being generated by the merging of two firms, such mergers are essential to the competitive functioning of the market for corporate control. The possibility of takeovers is an extremely effective device for assuring significant competition for managers' positions. They are thus spurred to act in the shareholders' interest. And if they do not, the shareholders will benefit from competing managers' buying up their stock at a premium over its market price.

An understanding of the market for corporate control lays to rest most of the hoary bugaboos about the "separation of

ownership and control" that have plagued our corporation laws since Adolf A. Berle, Jr., and Gardiner Means popularized that concept 50 years ago in their famous work, *The Modern Corporation and Private Property.* Berle and Means correctly pointed out that in the form of business ownership known as the corporation, the stockholder-owners have no active voice in corporate decisionmaking. Much has been made of this in the ensuing years, and while it has been pointed out that the arrangement is suitable precisely to investors who wish to provide capital but *do not* have to be involved in management, many laws have been passed to make sure that corporate directors and managers don't use the firm's assets to serve their own interests at the expense of the shareholders'.

An understanding of the market for corporate control lays to rest most of the hoary bugaboos about the "separation of ownership and control."

In fact, though, the best thing the courts and lawmakers can do to protect shareholders is to allow competition in the market for corporate control. By stifling the market, with antitrust laws and other measures, they protect from significant competition those individuals currently functioning as the managers of stockholder-owned companies. The fact that those managers do not *like* competition for their positions—while enthusiastically praising it elsewhere, of course—certainly does not argue against a change in government policies. After all, who does like competition for his position?

But the opportunity for the executives of one corporation to pay a premium to the stockholders of another corporation to induce them to accept a merger is vital to the market. This transaction with shareholders is the primary protection our economic and legal systems offer against poor management, since the holdings of individuals are generally too small to allow them to rid a company of a managerial team that has caused stock prices to decline.

A buyout offer made by another corporation, which is itself subject to the same capital-market discipline, is also the best evidence (not perfect, but the best) that a change in the control of the assets of the target firm would improve economic efficiency. So takeovers not only protect shareholders against managerial abuse; they also enhance the efficiency of the economy's distribution of resources, including managerial talent.

The incumbent managers of a firm can and do construct roadblocks against a tender offer. Some of these defensive tactics may be useful in ensuring that shareholders get an appropriate price for their shares. But it is hard to believe that antitrust claims of the sort frequently used to fend off takeovers honestly reflect any legitimate concern that target company managers have either for their own shareholders' or for society's welfare. One can just imagine how incumbent managers could use a vague "public interest" rule to protect themselves from being replaced by another management team.

The case is no stronger—albeit less ironic—when the government sues on antitrust grounds. An FTC or Justice Department decision to prevent a merger implies that government lawyers and economists can know more about the business desirability of a specific merger than can the parties involved. For, even assuming that a merger gives some monopoly power (usually a heroic assumption), this merely reflects the "cost" side of the transaction. But there is also a "benefit" side—the benefits to be derived by all shareholders from active and unrestricted competition in the market for corporate control.

The pernicious effects of the government's antimerger activities under the antitrust laws are compounded by the securities laws. Current federal securities regulations significantly increase the purchase price of target firms. This decreases returns to acquiring firms and reduces the volume and productivity of takeovers. Hence, an unknown number of productive takeovers are deterred, and the takeovers that do occur produce smaller social gains.

It is common sense that stockholders are better off when offered a premium for stock that was selling for less before a tender offer. But it has taken imaginative, sophisticated statistical studies by financial experts to drive home the point. The results of research by economists at leading universities like Chicago, Rochester, and UCLA can be briefly summarized: the stockholders of a target firm make a good deal of money from a tender offer; the stockholders of the acquiring firm also realize significant gains, as their stock's price generally increases; and even if a tender offer is successfully blocked by the target firm's management, the stock declines in price but does not drop back to its pre-tender level.

Fans of monopoly theory may see such evidence as supporting the notion that mergers breed monopoly profits, but the facts do not bear this out. If a takeover increased the market power of the acquiring firm, the firm would be able to raise product prices (otherwise, why be concerned about market power?). But if this firm can raise its prices, so can other firms competing in the same industry. So the price of these companies' shares would also go up on announcement of a takeover, as the market reflected their new potential for higher profits.

In fact, however, analysis of stock-price data shows that the value of competing firms' stocks does not go up in response to a takeover bid. This supports the view that takeovers are evidence of competition in the market for corporate control and not of efforts to achieve market power. Likewise, government antimerger activities, such as ordered divestitures, have not been found to depress stock prices in the affected industry.

Takeovers are the primary protection our economic and legal systems offer against managerial abuse of stockholders.

The evidence also shows that mergers generally perform a beneficial function in reallocating physical resources from less-efficient to more-efficient users. And while some takeovers prove less desirable than the parties to the merger predicted, government authorities certainly have less ability to predict the results of any given takeover than do the parties involved or the stock market.

Contrary to popular worries, then, mergers and tender offers are not economically wasteful. Takeovers are not simply power games but reflect competition in a vital market, the market for control of valuable corporate assets. And there is no good reason for the government to interfere with the private, voluntary agreements that fuel takeovers. ◧

*Henry Manne is a professor of law and the director of the Law and Economics Center at Emory University. Among his numerous publications is "Mergers and the Market for Corporate Control" (*Journal of Political Economy, *1965), the basis for most subsequent scholarship on the market for corporate control.*

When George Stigler, as a young visiting professor, delivered his first lecture at Columbia College in the late '40s, the intellectual debate in New York City, reports Murray Rothbard, focused on whether official membership in the Communist Party was necessary for meaningful political activism. In that first address, Stigler detailed the counterproductive consequences of rent controls. He then exposed how minimum-wage laws create unemployment and discriminate against low-wage workers. The crowd was stunned.

Today, George Stigler can still shock his listeners, but now he can make many of them smile, as well. Stigler's critique of government regulation of business has spread so wide that, now, the **defenders** *of state intervention must explain themselves to incredulous crowds. In 1982, he even won the Nobel Prize in economics.*

When Stigler started out—first as a University of Chicago student in the '30s, then as a roving teacher before returning to Chicago in 1958—economists took large corporations' monopolistic power and consumers' manipulable desires as the foundation of market analysis. Stigler's relentless empirical work confounded the prejudices of his day. Among his many iconoclastic findings, for example, was that regulated stock-market returns in the '50s were no better than unregulated returns in the '20s.

"The study of the regulation of economic activity became a passion of Stigler's," UCLA economist Harold Demsetz recently wrote in **Science** *magazine. Stigler's "passion" soon led to perhaps his most famous paper—"The Theory of Economic Regulation," published in 1971—and his most important general hypothesis: "As a rule, regulation is acquired by the industry and is designed and operated primarily for its benefit."*

Contributing Editor Thomas Hazlett recently interviewed Professor Stigler at the Hoover Institution.

GEORGE STIGLER

REASON: What does a good economist contribute to society?
STIGLER: Well, what we mostly do is contribute maybe slightly better-trained minds to the society each June, and I don't think that's negligible. But just sticking to the research side, I think that we've done a very *good* job on the analysis of things like tariffs and energy programs. We're very good on whether a highway safety program makes sense or doesn't make sense, or at least what its costs and benefits are. And so forth down the line. We've been ingenious in our measurements and I think clear-headed in our analysis. It's not an accident that the president has a Council of Economic Advisers, although it seems to me to have too big a mandate for controlling the economy and not enough for these allocational things. I think the council's been a center of good sense through both parties on questions, for example, like minimum-wage legislation. The council has *always* fought next year's increase in the minimum wage. It's lost, because the AFL-CIO is stronger than the Council of Economic Advisers, but it's probably slowed down the growth, and I consider that a great service to this society. My friend Ronald Coase once said that if an economist delays the adoption of a bad law by one week, he has earned his lifetime salary several times over.
REASON: What government program would you most want to see abolished?
STIGLER: There's a long list of them. You understand that you have to draw a line between two different kinds of policies that an economist has a right to object to. One kind, he disagrees with the objective of the program. He says, "I'll be damned if I see why we have a great big protective system for domestic sugar producers." And here he's quarreling with Congress on whether that group is worthy of preferential treatment. And then there are lots of times when you name the policy, like clean air, where the techniques are very inefficient and undesirable. For example, in clean air we have a "nondegradation" policy. It says, don't let the air get worse in the terrible Ohio Valley, but don't let it get worse in the lovely, clean southwestern part of the United States, either. Well that's an excellent device to keep industry from migrating from Ohio to the Southwest, but it's not a device at all to keep air clean. It's a device to maximize the cost of that. Industries have to have expensive air scrubbers where there's no pollution as well as where there is, and so forth.
REASON: When you won your Nobel prize last year, you met with President Reagan. Did you give him any advice?
STIGLER: Feldstein [Martin Feldstein, chairman of the President's Council of Economic Advisers] kept urging me to say what the president should do. I didn't want to go into details, partly because in 20 minutes what difference would it make? The president was struggling to go off and meet the winner of the New York marathon race and stuff like that. But I said I thought we economists have two good functions that we can perform, including Feldstein, who is a very good economist. One is to say, "Well, Mr. President, here is a gang, the dairy interest, that's got a lot of clout and you've got to give them something. Let's figure out the cheapest way to give it to them." That's one important function of a professional economist, no matter what side you're on.
REASON: You should just accept the fact that this group has the political clout?
STIGLER: Yes, but then let's buy them off without what the economists call deadweight loss being imposed upon others.

And the other thing we can do as political advisors is to say, "Look, the industry structure is changing." Like the banking industry has been undergoing important changes. And those changes are the main reason for the deregulation, not Chicago School economists getting unusually eloquent. There are big divisions of interest in the industry, and big groups have been wanting to change sides. Whenever that's on the horizon—as it was in airlines in the late '70s, and as it has been in banking for five or seven years—if you can advise the president that that's coming, that's a great area to start deregulation. Because then half of the industry is going to support you. You're not fighting the battle of your life just for consumers, who tend not to be organized and not to support such efforts.
REASON: Why don't you grade the average American on his level of economic understanding?
STIGLER: By what standard? Should you grade them by comparing them to the best economist in the United States? Then I suppose the correct grade should be an F or F minus. But you know, so what? They lead useful lives, and they buy the amount of economic information that's appropriate for them to have. And they don't go home every night and say, "I wonder what Friedman wrote today that I can read." So I don't like to grade them that way. You see, if I had a way that they would enjoy learning more, then I really ought to become an entrepreneur and *do* it. If I had a nifty new cassette or a new magazine or something else that really gave them information that they'd like to have in a form they'd love to have it, I've got a fortune on my hands. I don't have to beg them in that case. But people *don't* want to go home every night and say, "Dear, do you really think that marginal-cost peak-load pricing would be better for our local electric utilities?" That *could* happen. But I don't even know whether the marriage would survive such strains!

PHOTOGRAPHS BY FRANK HANES

REASON: What's your view of the antitrust revisionism going on now—that the antitrust laws should be a lot more modestly applied?

STIGLER: Well, I've learned. The government had gotten more and more into watching all kinds of details like, "You have exclusive dealerships in selling bikes. Why, what right do you have to have that?" They were worrying about lots of details that I don't think were important, and in fact they're not even monopolistic. But now there's more and more an awareness that the real antitrust afflictions are horizontal combinations, or are mergers with monopolistic content.

REASON: Are Americans protected by public utility regulation?

STIGLER: When I did studies of this, the indications seemed to be not. In fact, there was a question whether the utility commissions were raising rates or holding them down.

REASON: A private monopoly unregulated by government would charge the same or lower prices for electric power?

STIGLER: That's right. We made studies for the 1910s and '20s. That's when the regulation really came in—there were still a lot of states that didn't have it. And what we did was to compare states and see whether, when you allow for costs of generation and things like that, the rate differences were appreciable. Well the differences weren't so large. We found that regulation, if it did anything, lowered the rate not for residences but for industrial users.

Now there's been a change in the last 10 or 15 years, partly due to fuel prices changing and partly due to the fact that in inflation, a new trend had taken place in electrical utilities. And a lot of the public utility commissions are dragging their feet and have been holding down rates. But studies indicate that these regulations which temporarily hold rates down have made investment unattractive. So the total cost of electricity is going to be substantially higher 10 years from now than it would be in the absence of regulation.

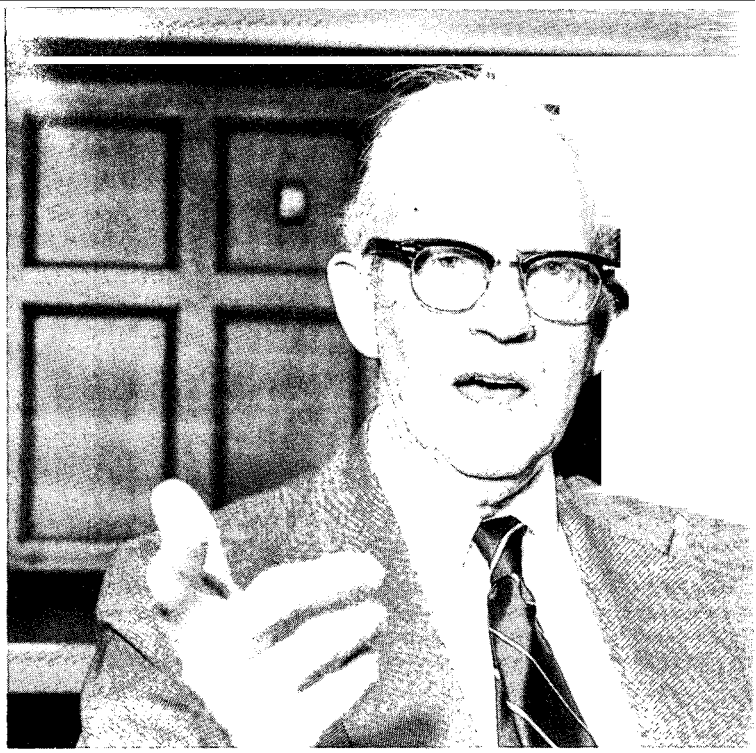
It's exactly the same as rent control. In the short run, clearly, if you had an apartment that was nice and well-built in Manhattan, you're better off with rent control—for 10 years you're going to have lower rents. But then you've got to ask the question: Who in their right mind is going to invest in that town? Housing in the long run in New York is going to be more expensive, since there's no such thing as a free brick and mortar construction.

REASON: Are you saying that without regulation, the electricity market was a competitive market like rental housing?

STIGLER: No. The utility field was partly monopolized by the states, you know, by exclusive franchises. But that's not the point. If I were a monopolist, I would maybe make more by charging enough to get a two percent higher rate of return than I would in the absence of regulation, or maybe I'd charge five percent more on prices. So that's a cost that you have, a social cost, of unregulated monopoly. But it's not at all clear that that cost will be anywhere near as large as the cost of an inefficient or very short-sighted regulatory system. It is quite possible that the "extortionate, self-seeking" monopolist would find it much more remunerative to have a big business and rapid innovation and cut prices, like the computer industry did for a long time. The computer industry is pretty competitive now, but even in the first 10 years of IBM's dynasty, the record of progress was incredible. That was self-interest—that wasn't benevolence.

REASON: So monopoly can be efficient?

STIGLER: Monopoly *should* be efficient. It isn't quite as efficient in taking account of the concerns of the consumer, but it's got to be efficient in production and innovation or it isn't making as much money as it should. The idea that the monopolist sits back and just clips coupons is nonsense. He's got all



"I have a feeling that intellectuals are like singers. If I say I want to hear only Wagner, they'll give it to me."

kinds of competitive pressures.

REASON: Then why this American preoccupation with antitrust legislation?

STIGLER: So far as I can tell, it's a public-interest law. If you propose an antitrust law, the only people who should be opposed to it are those who hope to become monopolists, and that's a very small set of any society. So it's a sort of public-interest law in the same sense in which I think having private property, enforcement of contracts, and suppression of crime are public-interest phenomena.

REASON: But the law has been used, for instance in the Alcoa decision, simply to hit against firms that were efficient and lowered prices to consumers but in doing so had out-competed a lot of rivals in the market that were consequently upset.

STIGLER: Well, you're simplifying the Alcoa case. The Alcoa case was partly that there had been suppression of international competition by joining in international cartels.

REASON: So you like the Sherman Antitrust Act? This is an anomaly.

STIGLER: I like the Sherman Act. I don't like the Clayton Act.

REASON: Why not?

STIGLER: Oh, it starts to get gimmicky there. It has dumb things in it like interlocking directorates that don't matter. It has a merger statute that I think is too severe, although I like it better than none at all. And it says, let's have a thing called the Federal Trade Commission, which took a separate act and which I would like in so many ways to see abolished. It's a nuisance. It's been petty. The current one is moving the other way, but it's got lots of terrible laws at its disposal.

REASON: What about advertising in the American economy? Is advertising some sign of monopoly?

STIGLER: No.

REASON: Of inefficiency?

STIGLER: You're almost getting close to what I did my work on, which should have, maybe did, win the prize for me—the economics of information. That is the area where I've done

"Ford collected a billion bucks making cars, but that was peanuts compared to the benefits to society."

probably my most important work as a professional scholar. Economics for a long time had a standard model in which it was assumed that people have perfect knowledge. And on this model, it's clear that advertising is manipulative and tends to deceive you and so forth and so on. So there was a very widespread, entrenched hostility to advertising among professional economists. And if you go through the literature up to 1960 or '61 when I wrote my article, and for some time after that...

REASON: "The Economics of Information"?

STIGLER: Yes. You would find lots of this hostility strewn across the landscape. But now economists have found that it's a fascinating area—does it make an important difference whether you and I have different amounts of information? and what competitive forces are there to stop exploitation of ignorance? and things like that. And now I'd say that the hostility to advertising is greatly diminished and the understanding of it improved.

In some ways it's a marvelous method of creating information. In areas like the local newspaper, the daily sales of the grocery stores, there isn't anything remotely like it in terms of efficiency and power in bringing about what we consider a well-organized market, which is a market where people are paying about the same prices for the same things.

REASON: What about some of the television advertising? How does the slogan "Have a Coke and a smile" help consumers?

STIGLER: Some very interesting stuff has been written on that by a former student of mine named Phillip Nelson. He says that if I advertise that I am the leading brand, whether it's automobiles or computers or cocaine or what, that conveys information to you—the information that a lot of people are using the product and are continuing to use it and that therefore it hasn't got palpable and serious deficiencies. And maybe that's the main clue you'll want at this moment. If I were to say to you, "Here are the engineering specifications of my car," you'd say, "My god, do I really want to know that much about a carburetor when I'm buying a new car?" Consumers have the problem, you see, of how to intelligently control their lives. If I can think up a method that will convey to them information that they can rely on as a guide and yet does not insist that they take postgraduate courses in three sciences, they'll be delighted. So one of the real searches in advertising is to try to communicate information of a kind that's relevant. The assurance of the continuity of the enterprise is one kind that's relevant. Now that's not the only kind. And statistical studies so far suggest that in fields where there's a great turnover, like cosmetics, advertising helps new products to get in pretty fast. So advertising opens up the market to new products and new brands, which is a source of potential strength to the system.

REASON: Let's turn to the larger picture. Is it the twilight of capitalism?

STIGLER: I don't think so. If it weren't for foreign military threats, we could go along one way or another with a very slow rate of increase of income with *all* the regulations on God's earth and no early demise of capitalism. It wouldn't be a very exciting or dynamic capitalism, but I'm not sure that it would come to a halt. Indeed, much of the problems of capitalism come from businessmen, from their own visits to Washington, not from having Ralph Nader run it over the rocks.

REASON: Visits for special favors?

STIGLER: Sure: "Bail me out. I want competition everywhere else, but for heaven's sake be good to the domestic textile industry," or "Be good to this other group," and so forth.

REASON: What is capitalism's constituency, then? Who's in favor of capitalism?

STIGLER: Oddly enough, aside from Chicago professors of economics, not as many as should be. In the long run, of course, workers and consumers are the main beneficiaries—easier jobs, higher incomes, and so forth. That's the main performance of the system. The businessman can make a killing, but it's a small killing compared to society's killing. Henry Ford made a lot of money making cars at one time, but that was a *small* advantage to him compared to the benefit to *millions* of people who for the first time in their lives were emancipated from common public carriers and could live where they wanted, move at the hours they wanted, to the places they wanted. Ford collected a billion bucks, but that was peanuts compared to the benefits.

REASON: Why is there such a preoccupation amongst some economists and almost all policymakers with the idea of equality of income?

STIGLER: It's been the predominant ethical creed of Western society for 100 years now, starting with the Fabians, at least. It's been the article of faith, to not have conspicuous, ostentatious, and even immoral inequalities in income.

REASON: Now it's interesting to hear you explain this penchant for egalitarianism in terms of what appears to be an intellectual acceptance, even citing the Fabians, an obviously intellectual group.

STIGLER: Well, I was going to say it's a creed. I normally don't place great faith in intellectuals as leaders, and I have to be consistent—or it's nice to be consistent, at least here. I think that the main thing is that the state turned out to be a splendid instrument for redistribution of income. It turned out, that is, to be highly available, in the sense that even in America where we had a constitutional code, amendments plus political moods led to great changes in what you could do.

REASON: It's pretty obvious that the state *can* rob Peter to pay Paul. But why has it been such a pervasive philosophy that in fact that's important?

STIGLER: Well maybe it's always been important. In one way you're asking a question that I don't think we have an answer to, and that is, Why has the state suddenly grown so much in the last 100 years? All the arguments I've given, and that a lot

of other people have given, have floundered in part on the problem that the state did not grow rapidly from 1750 to 1850. If anything it may have declined. And yet all the main kinds of historical trends, industrialization and so forth, were going on in both periods.

REASON: Could it be that the intellectual climate changed? The intellectuals turned on capitalism?

STIGLER: Well, that's Milton Friedman's answer. That's not mine. I have a feeling that intellectuals are like singers. If I say I want to hear Wagner, they'll give it to me. If I want to hear country and western or something else, they'll give it to me. And if I indicate that I want intellectuals to preach to me one line by buying their books and patronizing their lectures and appointing them to high office, they'll do it. And if I want them to do something else, they'll do it.

REASON: So you take the intellectual entrepreneur as more or less a passive reactor to the tastes and preferences of various economic interest groups?

STIGLER: Let me put it this way. Suppose there are two of us, and you're a pronounced social interventionist and I'm an anti-one. My name is William Graham Sumner, and yours is Thorstein Veblen or something. And neither one of us will change our views. We're men of the utmost integrity. The thing that will happen is the society changes. You're getting $800,000 a year in lecture fees and turning down a lot more, and I'm sitting in my barn occasionally muttering to a passerby that the world's going to hell. So you see, I'm not talking about dishonesty or anything like that.

REASON: But within the economic world, entrepreneurs don't simply passively react to consumer tastes. Henry Ford didn't, certainly. Mr. Edison didn't.

STIGLER: What do you mean? Now wait. Be careful. He wasn't passive. That's the wrong word to use. But I don't really think that Vasco de Gama went around the Cape of Good Hope and then after that England liked tea. We have latent desires. And now suppose the entrepreneur comes along. I've had a desire for household gimmicks which I can't quite specify now but which will be handy, like a method of kicking off flies in the room. And I don't articulate it, because I'm not an inventor. But the entrepreneur is searching around, and he tries 12 things, and 11 of them I don't want but that one I buy. He has to innovate to find out what my latent desires are, but he's not really creating them.

REASON: But isn't the intellectual simply doing that by advocating Fabian socialism or free-market capitalism or whatever the creed is?

STIGLER: But why did my desires now take that form in 1880 but not in 1810? I want to give a utility-maximizing explanation for that if I can. And it's a terrible thing, because you see most of the things in this world are not easy to explain, and yet I hope I have a principle if I were clever enough that would explain all of them. But most of the time if you ask why people got socialistic, for example, in the latter part of the 19th century, the intellectuals in particular, what kind of an answer would you get? I can't imagine what the answer is. It's completely ad hoc.

REASON: Joseph Schumpeter's theory was an economic theory of sorts, saying that a subsidized class develops out of capitalism. There is some sort of a preference on the part of the capitalist middle class to subsidize intellectuals, and these intellectuals inherently bite the hand that feeds them, because it is their interest to sort of propagandize for their own power to take over.

STIGLER: That's irrational on the part of these entrepreneurs. They're supporting potential intellectual traitors.

REASON: But it's only irrational in the long run if they in fact think that socialism is going to make their heirs poor. But they might have thought that socialism was going to make them wealthier. And in fact, a lot of people at the beginning of this century thought, and I'm sure quite sincerely, that socialism was a superior system in terms of material wealth. So why can't we just say that those people, given their limited information, were simply wrong, that they accepted what was in fact not in their best interest?

STIGLER: That's what I call the error theory. My complaint against that is, unless I manage to explain when errors are made and why and what kind, I have stopped all explanation; since one of the graceless things about errors is that they can come from anywhere and go in any direction. Of course I can say that the middle classes in particular were mistaken as to both the democratic nature of socialism and its humane nature, and as to its economic efficiency. And that explains that event. And then if socialism goes into decline, I can say that they saw through the error. And if it doesn't go into decline, the error persisted. And so...

REASON: That *is* a very frustrating way to analyze history. On the other hand, errors exist.

STIGLER: I think they do. I don't deny, for example, that the 1918 Prohibition amendment was an error. The American people were not prepared to abide by such a restriction. That means it was socially an error; it was an untenable policy. And I have no doubt some errors last longer than that. But in general the errors have to give way, it seems to me, to increased knowledge.

You see, if you play your error game, why did England overturn private enterprise on a wide scale, so that now this greatest of industrial nations and a very pretty civilization has a lower standard of living than even, let us say, Italy? What does it take to see through an error? So the error theory doesn't seem to me to help.

REASON: But you would have to argue that they are worse off overall for having adopted self-interested policies. So we both have trouble explaining it.

STIGLER: The only thing is that I'm prepared to continue to try to explain it on a principle. Whereas if you play the error game, you ought to start working on the question, What kinds of errors really are made and last? Nobody I know has tried that game. Milton Friedman, whom I greatly admire, says that the reason that India is crazy is that it got emancipated when Harold Laski was in the rider's seat in the West as an intellectual, whereas Japan got emancipated when Dewey walked around accompanied by good friends like laissez-faire economists and so forth and so on, and that's why Japan's been an economic miracle but India has been a shambles economically. I think that's an awfully simplistic reading of the role of the intellectual in life.

REASON: What is that role?

STIGLER: I'm still working on how to study the role of the intellectual. And my skepticism is not very popular with intellectuals. I understand that, since it's denigrating. In a way, I even have a slight streak of inconsistency in a related matter. I'm always complaining that we shouldn't be reformers, we should be scholars. We're more influential as scholars, because if we prove something, everybody believes it; whereas if we beg for something, they're skeptical.

REASON: The economist as preacher is ineffective, but the economist as scientist actually gets things done.

STIGLER: Very, very effective. And yet as a scientist he's obviously a reformer, too. He's trying to get the rest of his profession to change their tunes.

REASON: So that's the inconsistency?

STIGLER: It's a sort of one. Although there's this difference—that you try to get them to change, not by changing their case, but by demonstrating the superiority of alternatives. ◻

On the Road

(Continued from p. 40)

ting rates based on the cost of providing service. More than 40 percent of the surveyed carriers said that deregulation has led to lower freight charges. And, as might be expected, nearly two-thirds of them feel that deregulation has lowered their profits.

Just as shippers are a diverse group, so are truckers. And deregulation has not affected all carriers in the same way. Smaller carriers, for example, seem to be experiencing fewer negative impacts than larger carriers. And this runs counter to one of the purported justifications for regulation—the protection of the small carrier.

While more of the carriers surveyed said they would prefer a return to regulation than those preferring continued deregulation, there is an interesting divergence of opinion among subgroups. By a ratio of 3 to 1, unionized carriers who expressed a preference favored reregulation. But carriers who use independent owner-operators for providing service were evenly split on this issue. (One outspoken trucker, in responding to this issue on the survey, asserted that "truck regulation is stupid, costly, and unnecessary. All my experience in trucking has shown that the regulators know *nothing* about regulating.")

The positive results of deregulation in Arizona parallel those in Florida. While Arizona went through a lengthy legislative, initiative, and delayed implementation process, Florida lapsed into deregulation in 1980, when the state legislature failed to renew the regulatory authority of the public utility commission. Nonetheless, Beilock and Freeman report in their study for Arizona's Department of Transportation, the pattern of positive results was the same. Based on data from a 1981 survey of Florida truckers and shippers, a majority of users perceived increased competition. A third of them had been offered discounts. More than 60 percent had received offers of new service, and nearly three-fourths felt that rates were generally lower due to deregulation. The absence of a simultaneous hike in truck taxes may account for the more widespread impression of lower rates in Florida compared to Arizona.

From almost any perspective, Arizona's motor carrier deregulation has been a success. Based upon Beilock and Freeman's survey, users of trucking services in Arizona, by a wide margin, appear to prefer the deregulated environment. Overall, nearly 3 out of 4 of the surveyed shippers and receivers favored continued deregulation. Urban users favored deregulation by more than 4 to 1; rural users, by more than 2 to 1. Large shippers and receivers, Beilock and Freeman's survey found, favored deregulation by 4 to 1; small shippers and receivers, by 6 to 1.

Despite the overall success and popularity of motor carrier deregulation, attempts to chip away at it are under way. For example, in early 1983 Arizona passed legislation to reregulate ambulance service. The rationale was the typical "public health is too important to leave to the free market." Ironically, it was the previous regulatory regime that denied the establishment of new ambulance services. In a case that reached the Arizona Appeals Court in 1972, a firm applying to provide new ambulance service in a small town was denied authority, because other ambulance services in the nearby area were getting poor financial returns. The new firm's evidence of the established firms' slow service, the court decided, was insufficient to overcome the importance of the financial evidence of poor returns. The regulators and the court never considered the possible link between slow service and low profitability.

The second front for reregulation is in the taxi industry. Taxi availability in Phoenix has improved dramatically since deregulation. The official figure for taxis (not including "gypsy" cabs) in Maricopa County, which includes Phoenix, is 498 for 1982 compared to 251 prior to passage of deregulation legislation in 1979. In 1981, the year before deregulation went into effect, there were 341 cabs registered in Maricopa County. Undisclosed in these figures is the shift of actual cab operations from peripheral areas of the county to Phoenix—particularly to the airport. Thus, all factors considered, the amount of service available in Phoenix is probably three times what it was prior to 1979. And waiting times for cabs, consequently, have gone down substantially.

Passengers may pay fares higher or lower than under the previous, regulatory regime, depending on the taxi company they choose. The overwhelming majority of riders, it appears, are coping quite well with sometimes having to negotiate fares with drivers. The only information on dissatisfaction is that the city has "received some complaints." The alleged sources of these complaints are motel and hotel operators. (There is nothing, however, to stop these people from either establishing their own taxi service or "endorsing" taxi operators that meet with their approval.) In the face of all this, the city has been attempting to reimpose some sort of controls.

Those urging new taxi controls often cite tales of naive tourists having been ripped off by excessive cab fares. But these tales lack credibility. Over the long run, in an open market, high-priced cabs cannot exclude lower-priced cabs—consumers will seek out cabs offering lower fares.

Consider the situation at Phoenix's airport, the presumed site of these "rip-offs." There, taxi service is a hotbed of competition. Arriving travelers must pass posted notices that taxi fares may vary. Cab charges are routinely posted on the outside of the vehicle. There is no system requiring would-be riders to take any particular cab. They may choose from any that are waiting. In addition, the airport is also served by bus and limousine, not to mention numerous auto-rental companies. Only gross negligence on the part of a taxi rider could account for his paying more for a ride than he might have wished.

A TV station's touted exposé of these alleged rip-offs, conducted only months after deregulation went into effect, could produce "evidence" of overcharging only by *offering* drivers large sums for short rides. The TV station did not find any cabbies who *demanded* $20 or $30 for the few miles' ride to downtown. It was only when a "decoy" *offered* to pay these amounts that reporters were able to obtain "proof" of excessive charges.

Yet based on this flimsy case of the "defects" of deregulation, Phoenix city officials are seeking ways to reregulate the taxis. Their first attempt—in which the city limited the number of cabs allowed to serve the airport—was overturned by the Arizona Superior Court in early 1983, but on rather narrow grounds. It remains to be seen whether the city will try again to reregulate cabs.

Arizona is a state reputedly more committed to free enterprise than most, and the implementation of radical motor carrier deregulation can be taken as a demonstration of that commitment. But Arizona's experience also demonstrates that even widespread commitment to—as well as widespread satisfaction with—deregulation can be threatened by those special-interest minorities who seek to use the coercive engine of government to achieve ends unattainable through voluntary means. As with all basic freedoms, then, it remains clear that the price of economic liberties is, and always will be, eternal vigilance. ◻

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VIEWPOINT

The Truth at Stake

BY JAMES DALE DAVIDSON

Okay, it's pop quiz time. Can you identify Joan of Arc? Time's up. If you said that Joan was "the Maid of Orleans"—a poor peasant girl who rallied France militarily during the Middle Ages—you're wrong. If you added that she was a "saint" who was burned at the stake, you're still no more than technically right (about the saint part) but dead wrong about the burning. Sorry, you don't win the refrigerator.

This example provides delicious proof that you can't believe what you read in the papers (or even in the history books). Not when some powerful group has a strong incentive to concoct evidence and analysis to make you think that essential relationships are other than they are.

Back to Joan. No peasant, she. It turns out, in fact, that she was the daughter of Queen Isabeau of France and Louis d'Orleans, brother of Charles VI. (The good king was a bit mad, which may explain either why or how his brother came to father his wife's daughter). Joan was a princess—illegitimate, perhaps, but a princess nonetheless. Which goes a long way toward explaining how she was able to appear on the scene in the dramatic way she did and why she was so eager to have the Dauphin Charles crowned king. He was her half-brother (and perhaps even her three-quarters-brother, if one wants to be genetically precise).

Alas, her enthusiasm for the cause was impolitic, as a number of French historians have now sorted out—from the safe distance of 550 years. By insisting that her brother be crowned king, she was gumming up negotiations between Charles and the Duc de Bourgonne. More or less like a Jesse Helms-type pushing for "victory over communism" when the Republican president is seeking reelection on the strength of arms-control negotiations.

Joan was captured and tried and condemned by the Inquisition. As a princess, she could not be executed; so she was taken secretly to Rouen and held there until a peace treaty was finally concluded between her brother and the duke. Soon after Charles VII entered Paris in April 1436, Joan turned up near Metz. An archivist has actually uncovered a safe-conduct for Cologne made up in her name in 1436—five years after she was allegedly burnt at the stake. (The hooded woman who was burnt that day probably *was* just a peasant maid, which is why no one has ever heard of *her*.)

Enough five-century-old gossip. What shines through is the sparkle of truth, so mucked over by politically inspired distortions that its ever coming to light is a

miracle. As a conservator of the Bibliothèque Nationale said, it "seems to be veiled behind one of the greatest acts of mass brainwashing...of the past few centuries." (Only a librarian would refer to events in the 1430s as of "the past few centuries," as if he were talking about something just around the corner; but let that go.)

The thing to hold onto is the realization that mass brainwashing is going on constantly. Around the clock. It's not merely done by big shots in medieval courts. It's everywhere. Before most events can be understood, the facts must be ironed out, got at in roundabout ways. And most people, who cannot spare time and attention for doping out the truth, will be as gullible as French school children listening in their classrooms to the legend of Joan the Maid, simple peasant who could hear the whispers of God.

One gets the same sort of fantasy every morning in the *Washington Post*, but on a hundred different subjects so dull that no one will ever sell the movie rights. From London comes word that some character, who once made a living as the secretary of the Anti-Slavery Society, has come to the startling conclusion that there is slavery in London. In Mayfair, even. He probably really believes it. Then there's more drivel from Hobart Rowen about the evils of airline deregulation. He's armed with charts and diagrams to "prove" how the consumer is being stiffed, all kindly prepared by soon-to-be-unemployed airline economists. People *believe* these things.

Thousands of public-relations experts are employed directly by the government to cultivate the perception that whatever its agencies do is indispensable. Who's going to bother spending hundreds of millions to show otherwise? Answer: Nobody. The flacks in Washington could get somebody sainted—as was done with Joan in France earlier in this century—if there were a political advantage in it. (They have to be careful of the Baptist vote.)

The way most people see life—at least in its distant and abstract relationships, such as those involved in politics and the economy—is the product of a sad arithmetic. Sound, dispassionate analysis plays little part in it. When the Food and Commercial Workers go on strike, they tell the whole world not to buy Chicken McNuggets. "They're made in unsanitary conditions!" The same process produced *The Jungle* and the perception that free markets lead to putrid meat. Every USDA inspector in Chicago could be certifying that swamp possum was fancy-quality ground sirloin—and it would be 500 years before patient historians could sort out the truth. Such is the profound imbalance of incentives. There is no countervailing group of "un-inspectors" whose descendants will find employment "un-inspecting" the alleged failures of the market.

We ought to rephrase John Maynard Keynes's famous exaggeration about the influence of ideas on events. Mad men, or mad maids, who hear voices in the air don't distill their frenzy from defunct economists. They're just suckers for a press release.

Jim Davidson is founder and chairman of the National Taxpayers Union and the author of The Squeeze.

ILLUSTRATION BY SUSAN SALLADÉ

Deduct Your Vacation?

BY TIMOTHY CONDON

As any tax specialist can tell you, certain areas of the tax law are "hot" at any given time. When Congress tinkers with the basic revenue laws—as it does virtually every year these days—tax professionals pounce immediately and figure out all the new angles to save their clients money. Of course, as soon as it becomes apparent to the IRS what's happening—that somehow, somewhere, a taxpayer is saving money—a counterattack is launched. Usually the entire issue is resolved in the federal courts, from the US Tax Court on up. Sometimes the IRS can't win a victory there and turns to Congress to get the law changed, as with the vacation-home tax break that so many taxpayers were enjoying in the 1970s.

I can see the waves building on the newest "hot" area of the tax law. Before it's all over, a whole bunch of taxpayers are going to save lots and lots of money. The tax angle? Combining tax advice and information and return preparation with...well, let's call it a "working vacation."

Investment seminars in places like the Bahamas, Hong Kong, Costa Rica, and Switzerland have long been popular. The entire cost of such seminars, including getting there and back, is deductible—a fact that is widely advertised. Section 162 of the Internal Revenue Code allows deductions for this as well as for business conventions. The purpose of the convention or seminar, usually held in some wonderfully exotic place, must be related to a person's trade or business or to the "management, conservation, or maintenance of property held for the production or collection of income."

This area of the tax law is excellent for business people and investors and has been well used by them for years. Keep it in mind as you go about your own business and investment life. But it's not the area I'm talking about.

There's another section of the Internal Revenue Code, you see, and you don't have to be engaged in a trade or business or investment activities to take advantage of it. All you need to be is an American and taxed nearly to death, which all Americans are. (Incidentally, did you know that US citizens pay a much higher percentage of tax on their incomes in "capitalist" America than do the citizens of socialist France?)

I'm speaking now of Section 212 of the tax code, a section that seems to be taking off lately. It says that any expense related to "the determination, collection, or refund of any tax" is deductible. Well, hell, whenever you get with your tax advisor to scheme up some new tax-saving strategies, that would seem to fit. Not to mention when you actually sit down with your tax champ and *prepare* your tax return. Hmm-m-m-m. Nice break. But most people only drive a few miles once or twice a year to do such things; the mileage is deductible, as is the fee, but that's peanuts...compared to getting together with your tax preparer in some faraway spot. Nice, hah? Or say you're just attending a series of tax *seminars*. That's related to "determination" of your tax bill, isn't it? If you're learning all about how to *reduce* the ugly specter of paying taxes, wouldn't that qualify?

At least one "Big Eight" international accounting firm thinks the answer is yes—and is teaming up with a resort enterprise to make the best of it. The Denver office of Touche Ross & Co. is offering five-day Super Saver Tax Holiday Seminars this winter. On each day, there will be a 1½-hour session in the morning and another in the afternoon—and it's happening in some of the best ski country in North America. They don't *guarantee* that the entire cost of the trip will be deductible, mind you, but the entire plan is set up to maximize that probability under Section 212(3).

Predictably, the IRS has already started grumbling. Some of the tax bureaucrats have said that "it all depends." You have to spend a good chunk of time learning about and discussing personal-finance and tax strategies; and the "dominant reason" for taking the trip has to be tax/finance-related. Otherwise they'll disallow the deductibility of the travel. And they just might, in *any* event, demand what's called an "allocation." You have to divide your time spent on the trip into tax/finance (deductible) and non-tax/finance (*non*deductible) portions. If you don't "allocate," the favorite tactic of the IRS is to refuse any deduction at all. That will be their predictable attack.

In any event, it appears that at least a portion of any such trips will be deductible (no, we won't be able to deduct our ski-rental or scuba-diving costs). And if the trip is "primarily" related to tax and finance, then the cost of getting there and getting home should be entirely deductible—just as with business and investment conventions.

Now, most of the above will be attractive only to the Big People. After all, *they're* the ones with the bucks, and they have to know how to save, 50 percent tax bracket and all. What about us Little People?

Maybe, my friends, you should all consider locating a tax specialist somewhere *else* in the country? Somewhere you'd like to visit a couple of times a year? You know, skiers go to Colorado; divers, sailors, and sun freaks to Florida; museum and art buffs to New York or Washington, D.C.; Easterners like to visit California; West Coasters like to take a break from the craziness, say in Maine or North Carolina; and so forth.

Does everybody get the picture? How do you go about finding a tax helper in a far-off land? Ask anyone you know who lives there. Or get a current phone directory for that area and make some calls. Visit in the middle of the year and talk with a few tax advisors. Select one you like—one with the right attitude about the subject of this column, for example.

One last thing: if you're going to do it, do it now, because the war is going to heat up fast. Pretty soon everyone and his sister's going to be taking advantage of the situation—as they should. The IRS will counterattack with a heavy propaganda barrage, new disclosure questions on the tax-return forms, and in court. If they can't get their way in court (and they shouldn't, given the state of both the statutory and case law), they'll go to Congress. And Congress, being the way it is, just might give the tax-guzzlers what they want.

So join the fray right away. Fly the friendly skies of the Tax Deductible Vacation. Your tax specialist is ready when you are. Or, he or she had *better* be ready!

Tim Condon is an attorney and tax specialist practicing in Florida.

SPOTLIGHT

Resourceful Writer

BY PATRICK COX

Julian Simon has managed to make a living doing practically nothing that he trained to do. He is, first and foremost, a writer; but he is known mostly as an economist, though he has no formal economic training. At present he is a professor of economics at the University of Maryland and a senior fellow in resource economics at the Heritage Foundation. His expertise is in immigration policy, and he has emerged as one of the most skillful and persuasive critics of immigration restrictions. But his background is by no means irrelevant to his work.

The Navy ROTC sent Simon to Harvard to do his undergraduate work in experimental psychology—an experience he calls "a mixed blessing." After three years in the Navy, he almost went to medical school but instead went to work as an advertising copywriter. He then put in six months at Ziff-Davis Publishing, selling and promoting magazines.

In 1957, Simon decided to get an M.B.A. at the University of Chicago but ended up with a Ph.D. in business three years later. His thesis was in university-library management, so, typical of Simon's quixotic career jumps, he set up a mail-order business.

Several years later, he was teaching advertising at the University of Illinois but realized that writing was what he liked most. So he decided to dedicate himself to it. "I realized then that I was a writer, but I wanted to be both a writer *and* a scholar. Research—grubbing for facts, ideas, theoretical formulations—is part of that process.

"My experience in business played a great part in my approach to economic problems," says Simon, "partly because you can't be in business without seeing that there are all kinds of problems that aren't in economic models. In a way, I have benefited from my lack of economic training, because economists tend to approach problems from a scientific point of view. Scientists try to explain some puzzling aspect of nature, while people in business, like engineers, are more interested in finding the consequences of changing some variable."

Simon's first scholarly work—mostly critical—was on the economics of advertising. (And Simon was the first to do statistical work leading to the estimate that smoking one cigarette shortens your life by 5 to 9 minutes.) His second book was a "how to" book on research methods for social scientists, and his third was another book on advertising, which ended with the conclusion that too much research had already been done on the subject and that the really important issues are ethical and aesthetic.

In the past few years, Simon has changed his mind about advertising,

JULIAN SIMON

largely due to the influence of free-market economist Friedrich Hayek. "Some sorts of advertising are very important," Simon now says, "such as classified and industrial, and the rest is irrelevant and not an important area of inquiry."

His interest in immigration started during the population panic of 1969-70. He read a *New York Times* article on the population explosion and "enlisted in the good fight to stop it, using all my marketing skills." But, being a meticulous scholar, he researched the subject and came across Simon Kuznets's work on the subject. "He was my first real teacher," says Simon, "even before I ever met him." Simon kept his zeal for the population issue, but he wrote from a point of view exactly opposite that of the Malthusians, who were convinced, says Simon, "the world would shortly go up in flames."

Simon's groundbreaking work on the population issue was treated with hysterical indignation and accusations. He even admits to one fist fight with a prominent so-called scholar. And as he dealt with one issue after another, explaining each into irrelevance, others were raised.

He says, "I was led from living space to resources to forests to water and on and on. There is no end to the objections people have to increased immigration." His main scholarly work on the subject is *The Economics of Population Growth*, published by Princeton University Press in 1977, but it was *The Ultimate Resource*, a less-academic work published by Princeton in 1981, that really shook things up. Its reception "exceeded my wildest expectations," Simon recounts. "The best part was the screams of the environmentalists. They assailed both my motives and my intelligence."

Simon likens his sudden entrance into the public eye to a bum sneaking into a posh Manhattan restaurant and being greeted with a magnum of champagne and a cigar. And he is still enjoying his new-found influence on immigration thinking. "Within the range of human experience," he says, "there has never been an influx of immigration that was too much for society to handle. There are really no good reasons for restricting immigration, and there are excellent reasons for allowing it."

According to Simon, many of the reasons people oppose immigration have more to do with psychology than economics. Part of the problem, he says, "is that moving but mischievously misleading poem by Emma Lazarus on the bottom of the Statue of Liberty. Immigrants were never tired, poor, huddled masses. The media are also a major problem, showing pictures of immigrants behind chain-link fences looking like caged animals. They never show pictures of the same people three months later, working two jobs to support their families while studying English on the side. Immigrants are, on the average, as well-educated as natives and actually contribute *more* to the social-welfare system than they take out. They are, in truth, the ultimate resource."

Patrick Cox is a frequent guest columnist for USA Today *and public affairs director of the Pacific Institute for Public Policy Research.*

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MOVIES

Reviewed by John Hospers

Testament

Testament begins, much like *Ordinary People*, with some happy incidents in the life of a "typical" California family—husband (William Devane), wife (Jane Alexander), and three children. Suddenly, without warning, comes news that the entire East Coast has been wiped out by nuclear blasts, and then San Francisco and Los Angeles. The small town in central California in which the scene is set remains, for the moment, relatively unscathed.

In TESTAMENT, Jane Alexander plays Carol Wetherly, a mother struggling to hold her family together in the aftermath of a nuclear war.

At first nothing much happens; school and work go on as before, except that there is no transportation and food must be rationed. But over a year's stretch of time the effects of fallout gradually accumulate: Many die of radiation sickness, including two of the family's three children. Soon there are no more physicians available, nor any electricity or fuel. No attempts to make contact with the outside world are successful. Increasingly people fall ill and die.

Jane Alexander, in a remarkably sensitive performance, tries to hold her dwindling family together amidst incidents such as friends stealing from each other. But in the end there is nothing, and we know that all will soon give up their struggle for life.

Everything is underplayed, as it was in a similar doomsday film, *On the Beach*. We are often left to infer what tragic events have occurred rather than being shown them. But the story is more remarkable for what it is about than for the way it is handled—not that the latter is inept or insensitive, only that it is not remarkable.

We are not told from what nation the blasts came, or whether there was retaliation—none of this seems to matter. (Apparently there were no follow-up blasts.) Nor are any solutions suggested. The film, though it will be used by "freeze" advocates (both unilateral and bilateral) to bolster their position, is just as compatible with a policy of deterrence to prevent such catastrophes as the film depicts. We are simply shown (with how much accuracy it is difficult to determine) what the aftereffects of a nuclear blast are, and then left to draw our own conclusions. It is doubtful that any conclusion already arrived at will be altered by seeing this film.

Tomorrow

A modest film likely to be lost in the scuffle is *Tomorrow*, based on William Faulkner's short story. Not since the remarkable but unremarked film of the 1950s *Intruder in the Dust* has a Faulkner story been so sensitively brought to the screen. Robert Duvall, in the title role as the Mississippi dirt-farmer whose exterior is so impassive that he never seems to have any emotions at all, is remarkable in an authentic and beautifully controlled performance. To see the repressed emotions inside him well up as he takes in a strange girl, assists at the birth of her child, and raises the child as his own when the girl dies, is a revelation to the viewer.

Tomorrow is filmed, as it should be, in black and white, but the black seems (whether deliberately or not) to be washed out and faded. Moreover, the film is primarily a mood piece, and there is so little action—or rather it is so slow in developing—that most audiences, not attuned to the sensitive portrayal of character, will tend to lose patience with it. But the fault is theirs, not the film's.

L'Etoile du Nord

L'Etoile du Nord is a little gem of a picture. It is framed around a murder mystery—but it is actually not much of a mystery, nor is there much suspense. The charm of the picture lies in the subtle interactions of the various characters: the middle-aged woman (Simone Signoret), moral, respectable, devoted to her husband, yet drawn strangely to the man who comes to her boarding house; the man (Philippe Noiret), who affects in different ways the lives of everyone there; the woman's two daughters, one a street trollop and the other, under-age, secretly sleeping with the house boarders; and finally the motley crew of boarders. Each of them is nicely individualized. Simone Signoret and Philippe Noiret give beautifully restrained performances in the main roles.

There is very little high drama and few dramatic confrontation scenes. Everything is understated, but the fine shades of characterization come out more effectively than in most American films. It is all done with minimal cues, which in most American pictures are either absent or so grossly overdone as to be too obvious. Though not pretentious, this is a study in human nature that rings true, and the combination of character and situation make it thoroughly enjoyable to see.

John Hospers is the author of Understanding the Arts. *He teaches philosophy at the University of Southern California and is the editor of the* Monist.

BOOKS

Inflating Taxation

Is Inflation Ending?
Are You Ready?
By A. Gary Shilling and Kiril Sokoloff
New York: McGraw-Hill.
1983. 256 pp. $17.95.

Reviewed by Tom Bethell

To answer the coy question in the title of their book, Gary Shilling and Kiril Sokoloff respond that, yes, inflation is ending...probably. I think they are right (probably), for reasons I have discussed in REASON (Viewpoint, May and August 1983). Nevertheless, there is much to disagree with in this book. Explorers may come out at the right place, but it does not follow that their map reading was impeccable en route.

The authors' main point, really, is that the principal cause of inflation is government spending. This is controversial, but in a very broad sense it is at least approximately true. Further, the authors are right to suggest that the electorate would like to bring spending under control; are fed up with politicians; think "balancing the budget" means cutting spending, not raising taxes; don't think government solutions work any more; and collectively are more worried about inflation than about unemployment.

(This last point was reaffirmed by Margaret Thatcher's impressive reelection in Britain last June in the face of high unemployment, at a time of declining inflation. The news media have been particularly remiss in trying to convince us that unemployment is more threatening to incumbent politicians than it really is.)

All these things I can assent to. Nevertheless, there is a stubborn, contradictory fact, which logically should have played havoc with the Shilling-Sokoloff thesis. President Reagan, elected to bring government under control, has not really succeeded at all. Government spending as a percentage of the gross national product (GNP) is now 25 percent, up from 22.5 percent when he was elected. In 1981 federal spending for fiscal '84 was projected at $758 billion. Now, two years later, we can see that it is going to be $100 billion higher than that, even though inflation has declined in the interim. Also, reductions in income tax rates have been offset at all income levels by bracket creep and Social Security tax hikes. A massive Social Security tax increase is taking effect on January 1.

In the face of this, anyone who believes, as the authors do, that "we can at least look forward to a reduction in the government's share of the economic pie as the private sector grows faster than government spending" is an optimist. Nevertheless, inflation *has* come down and may stay down. Why? An important reason, as the authors say, is that lenders were fooled by inflation for quite a while but are no longer. They now demand and receive a rate of interest that is higher than inflation. Real interest rates, the authors add, "will be kept high by uncertainty on the part of lenders....When a structural shift like this takes place, it takes some time to change it." True. And high real interest will prevent the inflation bird from getting off the ground.

Now, what about government spending? The crucial variable is not the magnitude of *resources* successfully captured by the government but the magnitude of general *discouragement* accompanying such capture. The authors never quite seem to grasp this. Government spending does *not* provide us with a true reading of the burden of government, although on average it may often reflect it. Very high tax rates, as in Bangladesh, can collect low revenues, and such governments can falsely appear to be imposing a small burden on the economy.

The authors write: "The federal government transferred purchasing power from the private sector to itself by putting excess demand in the economy, which was manifested by inflation. Then Washington paid for this rising spending by squeezing out of the private sector the expanded tax revenues that resulted from inflation."

I would have rewritten this: "The federal government transfers purchasing power from the private sector to itself by threatening to put people in jail if they don't pay up. If the government then tries to take too much money, people get discouraged and stop working. Fewer things are made, and those that are made cost more. Furthermore, if you believe Keynes's 'balanced-budget-multiplier' argument, you can also say that the transfer of resources from rich people's savings accounts to poor people's check-

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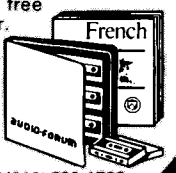

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ing accounts increases aggregate demand—which can be inflationary."

In short, it is high *taxation* that is inflationary, not (necessarily) high government spending. This has been well illustrated in the United States in the past three years. Spending has gone way up but taxation has not. Inflation has come down. Those who are curious about the future course of inflation should keep their eye on the Senate Finance Committee and the House Ways and Means Committee, where tax bills originate, not on the appropriations committees. It is the main weakness of this book that the authors fail to take note of the connection between inflation and taxation. They may think that government spending is a good approximation of, or "proxy" for, taxation, but that is incorrect. A country could have fairly high government spending, paid for by a combination of borrowing and low marginal tax rates, without any inflation.

On the other hand, the authors are correct to say that it is simplistic merely to blame inflation on "the money supply." It is true that a rise in the money supply will accompany inflation, but this rise is almost always the *response* to some other, prior problem that was the true cause of the inflation. The increase in the money supply is thus a kind of lubricant, oiling an economy whose gears are not meshing properly. Our position today, as the authors point out in different words, is that this monetary lubricant can no longer be rationally applied to the machine, because after so much use it now has perverse effects that merely exacerbate the original problem. It is no longer possible to push interest rates down (except for very short periods) by turning on the monetary spigots.

There are many other good things in this book, which I would recommend to all students of inflation, one of the great problems of our time. Nevertheless, the problems of government spending and taxation do need to be differentiated.

Contributing Editor Tom Bethell also writes for National Review *and* Washington Monthly.

Jeremiah or False Prophet?

Algeny
By Jeremy Rifkin
New York: Viking Press. 1983. 541 pp. $14.75.

Reviewed by Jane M. Orient

The founder of the Moral Majority, the president of Reconstructionist Rabbinical College, many Catholic bishops, and the president of the National Council of Churches have all en-

Book Hints

a selective mention of books received for review

While no one can ever be guaranteed a path to riches, expert investment analysts can help point the way. Where are the investment opportunities of the 80s?

In *High Tech Investing* (New York: Times Books, 1983, 283 pp., $17.65) Rodger Bridwell identifies money-making potential in six high-tech growth areas: mini- and microcomputers; computer-aided design and manufacturing devices; industrial and service robots; software programs; biochemical products; and ultramodern electronics. Overseas markets provide another frontier for American investors to explore.

In *International Investment Opportunities* (New York: William Morrow, 1983, 375 pp., $17.95) Adrian Day, an investment advisor and editor of a financial newsletter, analyzes a panorama of international investment opportunities. And a detailed account of Swiss banking and investment possibilities can be found in *The Swiss System: How the Gnomes of Zurich Can Help Your Assets Grow Safely and Confidently* (St. Thomas, Virgin Islands: Caribbean Overseas Enterprises, 1983, 196 pp., $29.95). *The Swiss System* features contributions by several leading Swiss banking and investment authorities as well as financial writers, among them Harry Browne.

For the reader interested in another area, *The Metals Investment Handbook* (Costa Mesa, Calif.: Common Sense Press, 1983, 171 pp., $25.00), by R. S. Taylor-Radford and John A. Pugsley, offers a well-researched review of industrial metals and their markets. On a less-exotic note, Gil Armen in *Residential Real Estate* (Englewood Cliffs, N.J.: Prentice-Hall, 1983, 301 pp., $9.95 paper) describes the benefits of investing in residential real estate in the 1980s and guides the reader through the investment process.

For those alarmed about all the recent talk about bank failures and their potential impact on investments, *When Your Bank Fails* (Princeton, N.J.: Amwell, 1983, 244 pp., $16.95), by REASON contributor Dennis Turner describes the scope and causes of current bank problems and suggests how individuals can protect themselves against a banking collapse.

Speaking of collapse, in the *World Crisis in Social Security* (Paris: Fondation Nationale d'Economique Politique; San Francisco: Institute for Contemporary Studies, 1982, 245 pp., $9.95 paper), edited by Jean-Jacques Rosa, various authors expose the international prevalence of the crisis faced by social security programs. Though the programs differ in details, they are confronting surprisingly similar problems.

For a look at welfare policies in general, David Green's monograph, *The Welfare State: For Rich or for Poor?* (London: Institute of Economic Affairs, 1982, 40 pp., distr. by Transatlantic Arts, Albuquerque, N.M., $4.75 paper) analyzes government welfare as a defective method of aiding the unfortunate.

Well-known medical journalist Harry Schwartz investigates and repudiates arguments in behalf of national health insurance in his monograph, *National Health Insurance* (Dallas: National Center for Policy Analysis, 1983, 56 pp., $5.00 paper). Another look at health care is provided by Clark Havighurst in his comprehensive critical assessment of regulatory policies in this field—*Deregulating the Health Care Industry* (Cambridge, Mass.: Ballinger, 1982, 500 pp., $37.50). Also arguing for free choice and free markets, Fred D. Miller, Jr., explores the infant formula controversy in *Out of the Mouths of Babes* (Bowling Green, Ohio: The Social Philosophy and Policy Center, 1983, 98 pp., $6.95 paper).

—L. S.

dorsed political gadfly Jeremy Rifkin's proposal to clamp down on biotechnology research: "Resolved, that efforts to engineer specific genetic traits into the germline of the human species should not be attempted." *Algeny*, the far-reaching moral and ecological argument behind this limited statement, should be required reading for all clerics.

Algeny is analogous to alchemy. Alchemy harnessed fire, enabling man to transform nature. Algeny applies cybernetics, allowing humankind to manipulate even living beings for its own purposes. Biotechnology marks a watershed as dramatic as the Industrial Revolution in which, according to Rifkin, organisms will be visualized as mere programs, "desacralized" along with the inanimate universe.

In Rifkin's view, to justify biotechnology as the next natural stage in evolution is to repeat Darwin's error of creating a model that simply rationalizes the evils of society. Darwin allegedly imposed his vision of competitive forces in England on the ecology of the Galapagos Islands. Rifkin attributes the acceptance of Darwinism to the eagerness of laissez-faire capitalists to certify their own morality, rather than to scientific evidence. In his murky theorizing about the origin of species, Rifkin postulates that species are "inviolate," thereby flaunting his ignorance of bacteriophage and other viruses, from which we learned about the transfer of genetic material from one species to another.

Although Rifkin's attack on evolution may appeal to fundamentalists, he has no more in common with creationists than evolutionists do. The Biblical story and the tree of life sketched by evolutionists both have the human species at the pinnacle, with nature organized hierarchically. Rifkin, however, believes that "all of life begins...[in] the place...where there are no hierarchies, no pecking orders, only relationships and mutual dependencies." Rifkin does like one idea from the book of Genesis—man must not try to become godlike by eating the fruit of the Tree of Knowledge. However, he sees in knowledge only the evil, not the good.

Like many who oppose research in biotechnology, Rifkin cites a parallel with the discovery of the atom's secrets. In his earlier book, *Entropy*, he explained persuasively why nuclear power is needed to support current population levels, while rejecting it all the same. Rifkin forgets that we don't need nuclear energy to level cities: Genghis Khan, the Roman legions, and the Royal Air Force did just as much damage as the Hiroshima bomb, though with greater human effort. Similarly, we don't need genetic engineering to have eugenics. Plato, Campanella, and Hitler were ignorant of gene sequencing. Their schemes required only an omnipotent government.

We do, however, need biotechnology to help feed the world, to develop bacteria capable of detoxifying wastes,

Jeremy Rifkin

and to manufacture monoclonal antibodies or superior vaccines. But all of these activities, like livestock breeding in Darwin's day, are profitable, not sacrificial.

Implying that he favors diversity and democracy, Rifkin raises the specter of an evil power engineering the human race, eliminating "undesirable" traits like problematic behavior. Someone who undertakes to advise Congress, as Rifkin has set out to do, ought to understand the difference between curing sickle cell anemia (an excruciatingly painful, hereditary disease caused by the substitution of a single amino acid in a single protein) and influencing complex characteristics like behavior. The still-speculative ability to do the first by no means guarantees the feasibility of the second. Nevertheless, Rifkin is willing to sacrifice the victims of genetic diseases, lest we risk extinction due to a germline that is too perfect; at the same time, he is supposedly opposed to "physical perpetuation at all costs." In seeking to halt advances in knowledge, not just specific applications of technology, what kind of government must Rifkin really support? Even the Spanish Inquisition failed to prevent the discoveries of Galileo and Columbus.

Jeremy Rifkin is no secular humanist. Possibly, that explains his appeal to religious leaders. Yet he is no Christian, either. Rather, he is the prophet of a new religion. "The resacralization of nature stands before us as the great mission of the coming age," he intones. We must acknowledge our debt of existence to the cosmos, by "sacrificing to the cosmos the measure of the sacrifices the cosmos made for us." Rifkin is not speaking of burnt offerings of pigeons and bullocks. "Pure sacrifice, collectively expressed and generationally sustained, has never yet occurred anywhere on earth." Even the Canaanites' sacrifices to Moloch had an ulterior motive, providing security for the future, which we must renounce. Furthermore, throwing a few babies into the maw of the idol would not suffice—Rifkin states unequivocally that a vast reduction in population is required for the "low entropy" age. The specific method is to be determined.

What apocalypse awaits us if we fail to give up the benefits of science? Our physics would hasten the heat death of the universe. As Rifkin cautions against hubris, he worries about fission reactors and forgets about stars. Our biology would make the world lonely "by stripping one living thing after another of its identity." Fulminating against Darwin's anthropomorphic "cosmology" early in the book, he ends with the immortal line, "The cosmos wails."

The plaudits of today's churchmen notwithstanding, a prophet of Israel would have recognized Rifkin as the idolater he is: "They prophesy unto you a false vision and divination, and a thing of nought, and the deceit of their heart" (Jeremiah 14:14).

Jane Orient is a medical doctor practicing in Tucson, Arizona.

Bridge to Freedom

Double Crossing
By Erika Holzer
New York: G. P. Putnam's Sons. 1983. 291 pp. $13.95.

Reviewed by Barbara Branden

Over the story of *Double Crossing* and over the lives of its protagonists looms the steel span of the Glienicker Bridge, a span that links—and divides—two worlds and three people. On one side of the bridge flicker the lights of West

AN UNDERGROUND LEGEND

VONU:
The Search For Personal Freedom
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Edited by Jon Fisher

Rayo was an early pioneer of libertarian theory. He coined the term "vonu" (invulnerability to coercion), and discussed non-political ways and means of achieving freedom here and now. His writings appeared in the late 60's and early 70's in obscure underground journals like *Libertarian Connection, Vonulife, Protos* and *Innovator.* Now Jon Fisher has collected together the best of Rayo's articles in one easily-accessible volume. *VONU* is an excellent example of the type of thinking necessary to break free and live your own life.

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REA93

THE RIGHT TO BE GREEDY

"The present forms of greed lose out, in the end, because they are *not greedy enough.*"

"Intelligence ends where morality begins. Morality ends where intelligence begins. Every moral is a psychic totem, a mental fetish-object, before which the moral fetishist subordinates himself, bows down, and offers sacrifice — indeed, offers *himself* in sacrifice. Every ideal is separated subjectivity; a part of the self separated off, ejected, frozen, and held *over* the rest of the self."

"In the end, egoism is our only friend; in the last analysis, greed is the only thing we can trust. Any revolutionary who is to be counted on can only be in it for *himself* — *un*selfish people can always switch loyalty from one projection to another."

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Berlin, beckoning between the concrete mounds of the Glienicker's watchtowers; on the other lies the gray, desolate terror of Potsdam, East Germany. On one side are hope, and freedom, and life; on the other, despair, slavery, and the blood-stains of murdered men who had dared attempt to escape their captors.

Moving inexorably toward the bridge, and toward the final confrontation that will be the climax of their lives, are: Adrienne Brenner, American, medical journalist—a woman to whom the issues of freedom and human rights blaze with a consuming intensity; her husband, Dr. Kurt Brenner, world-famous cardiac surgeon, sophisticated, opportunistic—a man terrified of the emerging secrets of his past; and Dr. Kiril Andreyev, citizen of Moscow, whose 47 years have been a single, patiently plotted, impassioned thrust toward freedom—and who will find, when he meets Adrienne Brenner, that his passion has intensified but his patience has burned itself out. It is on the Glienicker that Adrienne, Kurt, and Kiril will create the meaning of their pasts and seal their futures, as Kiril involves all three in his last desperate hope.

Erika Holzer has written a brilliantly suspenseful novel that lives and breathes her own passion for justice and the passion of totalitarian subjects everywhere for the freedom they are denied. *Double Crossing* is much more than a suspenseful political adventure, because it is told in intensely personal, human terms. In too many novels of East versus West, the reader feels he is reading a cops-and-robbers tale that could have been set in any place and at any historical time; but in *Double Crossing*, we see the souls of men and women who are free and the souls of men and women who live under terror.

We see those who have given in to slavery and given up, crushed by a system they cannot comprehend. We see those who embrace the system, choosing to create anguish in a vain effort to avoid suffering it. We see the brutes who willingly obey because they cannot conceptualize a different life. We see the day-by-day nightmare of life lived in a society in which even those most beloved cannot be trusted, in which even one's most private thoughts cannot be trusted. We see the gallantry of those who stand against the terror, clinging to the spirit of freedom. And, in the East-West medical conference that sets the stage for the story's final events—a conference that, like all such "exchanges," is staged for Soviet propaganda purposes—we see the treason perpetrated by free men when they appease totalitarian regimes and so strengthen the fist that hammers at human lives and hopes.

Impeccably researched, fast-moving, intricately plotted, *Double Crossing* (an alternate selection of the Literary Guild) is an important novel. I recommend it to all those who are concerned with liberty and to all those who seek fiction that translates the ideas of liberty into character, story, and suspense.

Barbara Branden, a former associate of the novelist-philosopher Ayn Rand, is currently writing a biography of Rand.

Water—An Impending Crisis?

Water Rights: Scarce Resource Allocation, Bureaucracy, and the Environment
Edited by Terry L. Anderson
Cambridge, Mass.: Ballinger; San Francisco: Pacific Institute for Public Policy Research. 1983. 348 pp. $35.00/$10.95.

Water: The Nature, Uses and Future of Our Most Precious and Abused Resource
By Fred Powledge
New York: Farrar, Straus, & Giroux. 1982. 423 pp. $14.95.

Reviewed by Steve H. Hanke

We have all heard about the nation's impending water crisis. Now we have two books that address this topic. Although both volumes deal with water, they do so with dramatically different styles and substantive arguments. Powledge's book is laced with analytical nonsense, but it is well written and retains the reader's attention. By contrast, Anderson offers a technically sound anthology that is, unfortunately, more powerful than most sleeping pills.

Let's first examine the arguments. Powledge opines that we are "running out" of water because we are either polluting what we have or wasting it. "Exploiters" are the problem. Of course, private industry is on Powledge's list. He characterizes the captains of industry as being, at best, amoral on the subject of water. Powledge leads us to believe that Love Canal was a typical private vice. (Absent from his references is REASON's careful dissection of government's role in

Only Way Left For Little Guy To Get Rich

Here Is the Uncensored Message My Wife Asked Me Not to Write

I love my wife. And I understand why she wants me to keep my mouth shut. She just wants to protect me from the IRS.

But I can't be quiet any longer. I'm angry. We are really getting jerked around. And I'm tired of it.

The government says one thing. Then does the opposite. Especially Reagan. And I even voted for him. One of my biggest mistakes.

First the feds talk tax cuts. Then they pass the biggest tax increase in history. Who are they kidding?

Average taxpayers, you and I, are getting screwed.

The new law doesn't bother the rich fat cats much. They still have loopholes galore. Let's face it. They always will.

But recently I ran across a workable angle. It's cheap. And it's legal. It's meant for the rich. But it's perfect for us little guys. You don't need any money. And we can get the same breaks the rich get.

I can hardly believe it. Catch this. I formed a corporation. Of my own. For peanuts.

It's my way of fighting back.

Now I have a small, one-man corporation. I operate out of my apartment. My work? I'm a commercial designer. Freelance. Brochures, fliers—stuff like that. On my income, I didn't think I could save much. But I'm paying almost zero taxes. And it's legit. Just like the fat cats do it. I have no guilt. Uncle Sam already gets plenty. Too much from all of us.

One thing the feds didn't bother much under the new tax laws—corporate tax goodies. Guess they figured right. Burden business too much. Result? No jobs for anybody. Including them. Not to worry. They know better.

From a buddy, I heard about this unusual book. It's called **How to Form Your Own Corporation Without a Lawyer for Under $50,** by Ted Nicholas. Damnedest book I've seen. Has the forms right in it. Pages are perforated. You just fill in some blanks and rip 'em out and mail them in. A couple of days later you've got a corporation. No wonder it's a best seller. (They tell me over 650,000 copies have been sold.)

No need to bring in other people. You can be President, Vice President, Secretary, Treasurer all by yourself. Just like me.

You know, lawyers charge $300 to $2,500 for incorporation. Talk about rip offs! And their secretary fills in the form—a single page with two blanks. Now you don't need a lawyer. And there is no hassle at all. It's simple. No wonder lawyers like you to think everything is so complicated.

You don't have to employ anyone either. Just by your lonesome. And I always thought corporations had to have lots of employees.

Oh well. Now I know.

Let me tell you something. I'm a skeptic. I like to shop by mail. But I've been ripped off in mail order. So, before I sent my check, I checked out the company. Called consumer and business bureaus. And the Chamber of Commerce. Found out publisher has a good record. And the book is guaranteed. So, what the hell. I spend that much on a few beers. That's how come I ordered it.

Damned if it didn't come in a couple of weeks.

I expected a shlocky-type mail order book. What a shock. Instead the book was typeset. Has a silver cover. And it's big. 8½ x 11.

I've had it for only three months. Already I've given myself all kinds of fringe benefits. Kind employer I am! Put in a medical reimbursement plan. A one-page form did it. Makes all my doctor, dentist and medical bills tax deductible—for me, my wife *and* my kids.

Now, my wife has been seeing a shrink. Guess living with me is no picnic. We deducted over $600 in the last two months alone. Also just got myself new teeth. Caps, I should say. Cost me $2,500. My son's braces figure to cost $2,000 next year. I can deduct it. Right off the top. And my wife and I are into special vitamins. Heavy. Those pills cost over 400 bucks. Couldn't get into them before because of cost. Tax-deductible now. Imagine this too. Right off the top!

Savings have been scarce for me. I have a helluva time saving bread anyway. But, with this little corporation, I'm really socking it away. How? First, I tax deduct any cash I don't need. A corporation makes this easy to do. And then I invest it. Interest and dividends are completely tax-free. Until I retire. In the meantime, I can even borrow the money back. So I don't lose the use of it like in an IRA or Keogh. This gimmick is called a Pension/Profit Sharing Plan. Again, I just filled in a couple of blanks on a standard form.

Now, I'm no financial genius. But I'll tell you this. I'll be a fat cat myself soon at this rate. It may not be as bad as I thought. Incorporation is the only way left. Now little guys like me have a shot at the big money.

This little corporation even covers my rear end. I could get sued. Everybody likes to sue these days. Something for nothing. And some judge might not like me. But you know what? The only thing anyone can get is what's in my little corporation. Big deal. A drafting table. A desk. And a little paper. Nobody can touch the real bucks. My home, cash, cars—even benefit plan monies are protected.

Maybe you've got some little business deal going. Or maybe you can get something started. Even a part-time business. This book can help. It can make the difference between just making it or operating just like the big boys. Even better, since you don't have their expenses.

For a real shot at big bucks, isn't it time you looked into incorporation?

It worked for me. So well that I wrote a fan letter to the company. They asked me to write this message. In my own words. But I did ask them not to print my name. Who knows? Maybe my wife is right. You can't be too careful. The IRS might want to hassle me. Even though everything is 100% legal. They may not like my message.

If you order now, the publisher will throw in a free bonus. A report called *The Income Plan.* Worth 10 bucks by itself. Shows you how to turn most jobs into a corporation. Outlines how to operate as an independent contractor instead of an employee. You can increase take home pay up to 40%. Taxes will no longer be withheld before you get your hands on the money.

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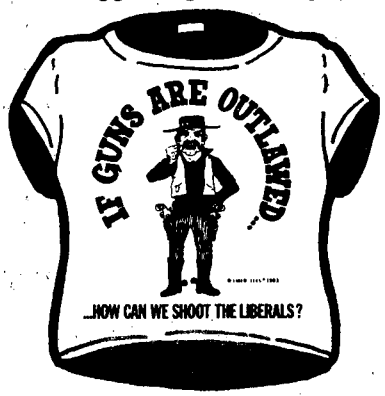

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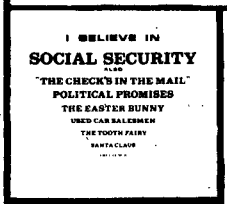

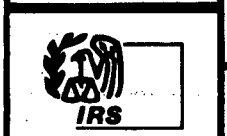

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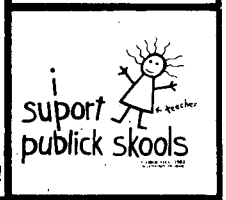

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the leakage of chemicals at Love Canal, in "Love Canal: The Truth Seeps Out," by Eric Zuesse, Feb. 1981.) Moreover, he argues that "Love Canals" are found at virtually every industrial site in the country.

"Corporate agriculture" is another major exploiter. The agricultural sector is responsible not only for poisoning our water supplies with pesticides and herbicides but also for depleting our groundwater aquifers by using them to irrigate submarginal land.

"Speculators" who specialize in second homes and the creation of suburban sprawl are also encouraging the exploitation and waste of our water resources. But if you think Powledge specializes in pointing a finger at the private sector, you are wrong. He also castigates the public sector for not enforcing the environmental laws, engaging in economically wasteful and environmentally damaging pork-barrel projects, and not maintaining its leaking urban supply systems.

Powledge's solution for the water crisis is a brand of neopopulism in which the people become "educated," "aware" and "involved" in a grass-roots movement to force "good government" on the federal establishment. If this is done, we are led to believe that the federal government will not fail. Instead, it will act wisely to regulate, manage, and ration our nation's water. Not surprisingly, Powledge's diagnosis of the crisis and its cure have a familiar ring; they can be found in virtually all the popular media.

What is not so well known is the fact that the propaganda mills of the Soviet Union are busy turning out the same type of "analyses." For example, Vitaliy Kobysh's essay, "Our Blue Planet," which appeared in the March 2, 1983, edition of Moscow's *Literaturnaya Gazeta*, tells us:

When you live in New York and other U.S. cities, and not only U.S. cities, you become accustomed to buying pure water in the supermarket, paying a substantial price for it. Everything is simple: money for a commodity. Yet water and air, like human sympathy or smiles on the faces of a passerby or neighbor, should not, cannot be a commodity. If they are a commodity, then everything mankind has achieved with his technical revolution is not only not worth a penny but is simply pointless. But let us return to water. It is no news to anyone that many rivers, lakes and seas are turning into sewage collectors and the world's oceans are being polluted with oil, radioactive waste and toxic chemicals. In the past decade the annual volume of sewage in the world was over 450 cubic km. About 6,000 cubic km of fresh water was expended to dispose of it, which is approximately 40 percent of all the world resources from rivers' annual flow.

Vitaliy Kobysh concludes that there is only one "path to man's salvation. It is paved by socialism."

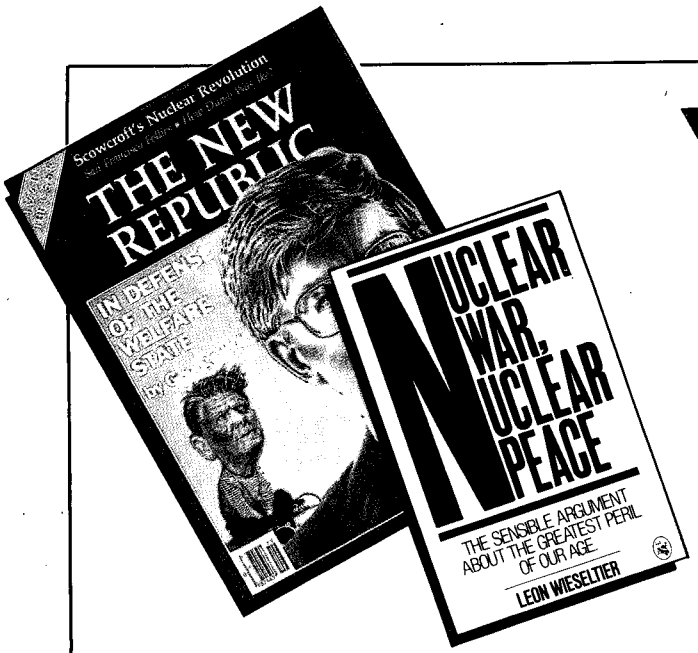
Karl Marx originally told us that capitalism would lead to pauperism. Since this assertion has not stood the test of time, the socialists and interventionists have changed their tune. Now they are telling us that capitalism will lead to environmental degradation and that a good dose of socialism will provide a sure-fire cure. Of course, they fail to disclose the environmental and health conditions that exist in socialist states.

Fred Powledge

Unlike former *New York Times* reporter Powledge, Anderson and Company fail to attract and retain the reader's attention. However, readers willing to expend the effort will find that this group of academics has done an excellent job of analyzing the problem. They clearly demonstrate that the lack of private property rights, ill-defined rights in water, restrictions on water transfers, administrative allocation and rationing schemes, price controls, and a host of other interventionist policies guarantee that water is not allocated to its highest and best use. This economic waste reduces the value of our nation's water resources.

Moreover, these interventionist policies create incentives that must lead to a crisis:

- Water is underpriced, which means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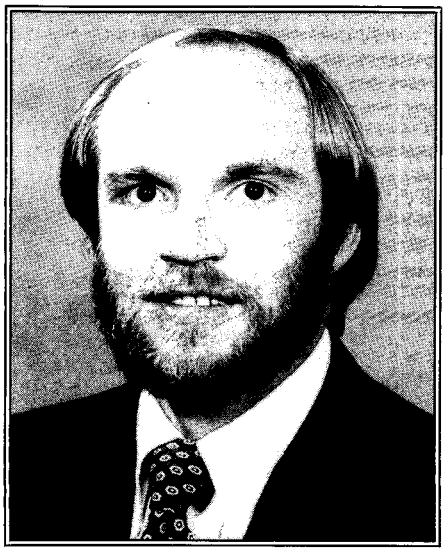
that the quantities demanded exceed the supplies offered.

- To fill this demand-supply gap, the government must use general revenues to subsidize additional private supplies or finance public works.
- As long as there are no constraints on general revenues that can be used for water development and as long as the water resources are available for development, there will be no crisis, although waste will occur.
- However, in a growing number of regions, we face either a general-revenue or water-resource constraint; hence, a water crisis.

For Anderson and his colleagues, the



Terry Anderson

solution to the water crisis is to establish transferable private property rights in water resources and to remove governmental intervention. What is interesting about the analytical, property-rights, and free-market arguments presented in *Water Rights* is not that they are new—these ideas have been around, even in the water resources field, for a number of years—but that they have had so little impact on water-policy debates in the past. It should remind us of Frank Knight's conclusion that the teaching of economics is so ineffective that we ought to give up and allow economics departments to be abolished.

What is really needed in the water field is a book based on the concepts presented by Anderson and Company and written in Powledge's style. This could influence popular opinion in a productive way.

Perhaps we should take the spirit of Knight's reflections seriously and begin to teach what Ludwig von Mises defined as economics in a manner that allows it to influence public opinion. For no policy, regardless of its merit, can be sustained without the support of public opinion.

Steve H. Hanke is a senior fellow at the Heritage Foundation and Professor of Applied Economics at the Johns Hopkins University.

Derailing the Regulators

Railroads, Freight, and Public Policy
By Theodore E. Keeler
Washington, D.C.: Brookings Institution. 1983. 180 pp. $9.95 paper.

Railroads: Their Rise and Fall
By Herbert E. Bixler
Jaffrey Center, N.H.: Bixler. 1982. 115 pp. $7.95.

Railroads: The Free Enterprise Alternative
By Daniel L. Overbey
Westport, Conn.: Quorum Books. 1982. 225 pp. $29.95.

Reviewed by Peter Samuel

The Brookings Institution is supposed to be the haven of liberals during periods of Republican administration. And these liberals are supposed to decry the free market and to want to enhance the power of the state. In the case of railroads, this might mean tighter regulation or more-extensive government ownership.

But there is also a genuinely liberal (in the English, Smithian sense of the word) streak at Brookings, and Theodore Keeler's book reflects that. *Railroads, Freight, and Public Policy* is organized and written in scholarly boilerplate. Actually, it is an extremely good applied-economics textbook and deserves a place in libraries on regulation.

In his history of railroads, Keeler makes the noteworthy point that railroad regulation by government and the courts predates the creation of the Interstate Commerce Commission (ICC) in 1887 and derived from medieval guild thinking, which favored cartel arrangements rather than market competition. The precedent for railroad regulation had been established with turnpikes and canals. Railroad companies got various privileges such as land grants, loan guarantees, and protection from competition; in return, they were subjected to all kinds of control over prices and service.

Keeler argues that the regime of controls had already been established in the states, but I think he goes too far there. A case can be made that supposedly rationalist regulatory bureaucracies such as the ICC are worse in disrupting and distorting the workings of the market than are corrupt politicians and judges imbued with guild protectionist thinking and engaged in making deals for their friends. After all, it took the ICC to put major railroads out of business, thereby inflicting Amtrak and Conrail on the taxpayers. The ultimately fatal power that the ICC exercised over Penn Central was its refusal to allow the abandonment of service on some 9,000 miles of money-losing track. Rarely did the Tammany Hall types in the states go so far as to kill the goose that laid their golden eggs!

The economists' major argument for such regulation in the past has been that economies of scale are endemic to an industry like railroads and make it a "natural monopoly" such that there will, in the absence of regulation, be destructive price wars. On this theory, the bankruptcy of the smaller road will be inevitable, so monopoly will inevitably result. Though Keeler's chapter on this is not one of his best, he does conclude that any economies of scale are insufficient to support the natural-monopoly theory in most instances.

The effect of regulation is to politicize an industry and to move prices away from costs. The politically strong get their charges reduced at the expense of higher costs or worse services for others, and economic inefficiency results. Freight is carried by the wrong mode, by the less-efficient carrier. Some production that is economic does not pay because of inflated transport costs. Other production, which should not pay because it is uneconomic, pays only because of the subsidization.

The losses of real income from regulation can become enormous. Keeler puts losses to the economy from the distortions of regulation at "well over a billion dollars a year" in the 1970s. He approves of the deregulation that has occurred so far but goes further, wanting the industry to be "freed of its medieval shackles of common carrier service obligations."

Herbert Bixler's book is the most compelling reading of the three, being a great piece of pamphleteering. It

has lots of anecdotes and plenty of examples and is well-written. Much of it is intriguing historical discussion of how a revolutionary technological innovation helped transform America, creating new industries and establishing new work habits and conventions (the four time zones were decided by railroad agents), but was increasingly blunted as a force for progress by politicization.

The 19th century, prior to detailed regulation, saw amazing advances in railroad technology and constant initiatives to improve service and efficiency and to lower costs. Standardization occurred where it was beneficial—standard couplers, rail gauges, clearance diagrams. Arrangements were made for coordinating through-trains and the interchange of cars and for processing waybills, so that nationwide service could be offered over many different railroads. By comparison, the railroads stagnated once detailed regulation was introduced.

In their innovative, expansive preregulation period, however, the railroad entrepreneurs became populist villains. "Robber barons" was their sobriquet. Stock frauds and corruption with politicians were so common that the verb "to railroad" came to mean the improper forcing of a privilege through the legislature. That, of course, is mixing politics with business, but was popularly taken as an argument for more politics.

In his final chapter, "What Might Have Been," Bixler suggests that in the absence of regulation we might have had high-speed passenger trains. Trains ran over 100 miles per hour in the 1890s, but if anything, train speeds have declined since then. And with adequate capitalization, modern trains and track, high speeds and service, the trains might never have lost passenger traffic the way they did to air. In the hothouse of regulation, labor unions were able to hamstring the industry with outrageous work rules and burden it with high costs. To this day, many freight trains are manned by five when one could do the job.

Innovation, adequate capitalization, reasonable costs—these might have kept business for the railroads, which has been lost apparently irrevocably to more competitive modes. Bixler hypothesizes that free railroads might by now have 150-mph passenger service and 120-mph freight service. Air travel would be less congested. Highways would be cheaper to build and more pleasant to drive on in the absence of so many long-distance trucks.

Daniel Overbey's book is the most dispensable of the three. It is pedantic and has only one idea in it—that the fixed way of railroad trackage should be owned by one entity and hired for use to other carriers who might own their own rolling stock or act in competition with other carriers, all on the same track. Railroads would be like highways, with a multiplicity of operators running over them.

The idea is feasible. Indeed, to some extent it is done now—by Amtrak! Over most of its mileage, Amtrak runs on lines owned by others.

Insofar as regulations prevent owners of tracks from hiring them out to others, or disposing of rolling stock, they should be abolished. There may be a good economic case for separate entities owning and maintaining track, and running trains, as Overbey says. It may increase competition.

But Overbey's is not necessarily a free-enterprise case. Genuine advocates of the free market do not lay down the rules about how industry should be organized. In doing that, Overbey is a planner, not a free-enterpriser.

Peter Samuel is a journalist with the Murdoch newspaper group in Washington, D.C. He taught economics in Melbourne and wrote on public policy for over 15 years for the Bulletin, *Australia's leading weekly magazine, and is a frequent contributor to* REASON.

LETTERS

(Continued from p. 8)

are just or unjust. In libertarian theory, processes which involve the initiation of force are unjust. In Marxist theory, justice depends upon whether a particular result is achieved; it necessarily follows that process constraints, such as individual rights, which impede the attainment of that result, are unjust. In other words, one cannot have both freedom, a process, and equality, a result. Ergo, Stalin.

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Further & More

GETTING GOVERNMENTS OUT OF CONTROL

Last May, John Doherty described various private-enterprise air traffic control operations throughout the United States ("Towering Entrepreneurs"). Now comes further word of private air traffic control overseas.

Most air traffic control in Britain is handled by a government agency called National Air Traffic Services. But according to H. J. Blanks, the head of Britain's Civil Aviation Policy Directorate, at a number of British airports (aerodromes) air traffic control is provided by outside contractors.

The largest such contractor is International Aeradio Limited (IAL), which is responsible for air traffic control at nine airports including Liverpool, Bournemouth, Humberside, and St. Mary's. IAL also provides extensive ATC services in other countries, mainly in the Middle East, and it operates a British school for training controllers.

Another private British air traffic control company—Airwork—services five British airports, including Perth and Exeter. Other companies provide air traffic control at one or two airports.

It's interesting that the airports at Bournemouth, Liverpool, and St. Mary's were formerly owned by the government. They began contracting out with private services not as the result of the Thatcher government's privatization efforts but on the initiative of local government bodies.

Meanwhile, Canada's union of air traffic controllers, the Canadian Air Traffic Control Association (CATCA), is pushing for privatization of that country's ATC system. In August, *Aviation Week* reported that CATCA recently formed a committee whose goal is to convert the nation's ATC system into a single corporation, a move that the union views as a step toward complete privatization. Two benefits of the single corporation, a union study determined, would be the streamlining of government control and the improvement of labor relations.

DEBATABLE FAIRNESS

The plot is thickening in the rift on the right over the Fairness Doctrine, which rift has some conservatives aligned with many liberals in support of the regulation. Mark Fowler, the deregulation-minded chairman of the Federal Communications Commission, wants to do away with the requirement that broadcasters cover all sides of controversial subjects and the opposing views of individuals, including political candidates and issues.

Fowler's hope, as we mentioned in December's Trends ("Freedom Program for Television"), had the conservative weekly *Human Events* all up in arms. The paper worried that without the Fairness Doctrine, broadcasters could become "as unfair, partisan or obscene as they desire." The conservative magazine *National Review*, on the other hand, printed some favorable words about repealing TV restrictions.

Now, in a later chapter of the debate, *Human Events* has followed a doctrine of fairness of its own. In October, the weekly published an article by Bruce Fein, FCC general counsel, in which he takes to task conservative Reed Irvine, of the news-monitoring group Accuracy in Media. A staunch Fairness Doctrine supporter, Irvine maintains that the doctrine is needed to block broadcasters from seizing political power by swaying voters, to ensure a broad airing of opinions, and to appease the public in their demand for unbiased broadcasting.

As for the fear of broadcasters seizing political power, Irvine simply is wrong in his assumption, Fein wrote, that "voters will mindlessly follow the political instructions of any broadcaster." In any case, Fein noted, broadcasters must compete with other broadcasters as well as other media—magazines, newspapers, books, and so on—in the marketplace of ideas.

A government-enforced doctrine of fairness depends on "an elusive concept that lends itself to manipulation," wrote Fein, whereas "eliminating the fairness doctrine would make [individuals'] detection of broadcast bias...easier." Moreover, he argued, "the proper remedy for bad counsel or biased viewpoints by broadcasters is good counsel and more speech, not government regulation." We couldn't agree more.

FIRE FIGHTING HEATING UP

In November, REASON reported on efforts to privatize fire-fighting services in two New England towns, Dover, New Hampshire, and Willimantic, Connecticut (see "Blazing Battles" by Jim Peron). The issue is heating up elsewhere, as well.

Lou Witzeman, founder of the pioneering Rural/Metro Fire Department in Arizona, has reported to REASON that the International Association of Fire Chiefs held a roundtable on privatization at its recent convention in Atlanta. Included in the discussion were some of the main figures in the Dover and Willimantic controversies. Chief Charles Monzillo of Willimantic was the chair, and other panel members included Chief David Bibber of Dover, George Zoley of the Wackenhut Corp., and—representing the "established fire service traditions and management style"—Chief Paul Roach of Stoughton, Massachusetts (a state that has passed a law prohibiting the contracting out of fire protection).

The representatives from Dover and Willimantic recounted their towns' experiences with the issue of privatizing fire-fighting services. Bibber, for example, told of the shift in his own thinking, "gradually coming from a neutral position to one in favor of the private sector." Zoley then briefed the audience on the history of private-sector fire fighting.

Witzeman also pointed out that Falck and Zonen, a Danish firm that provides fire-fighting service to the majority of Denmark's citizens, has now joined the Private Sector Fire Association, started last year in the United States. As he said, it gives the organization "a fine international scope."

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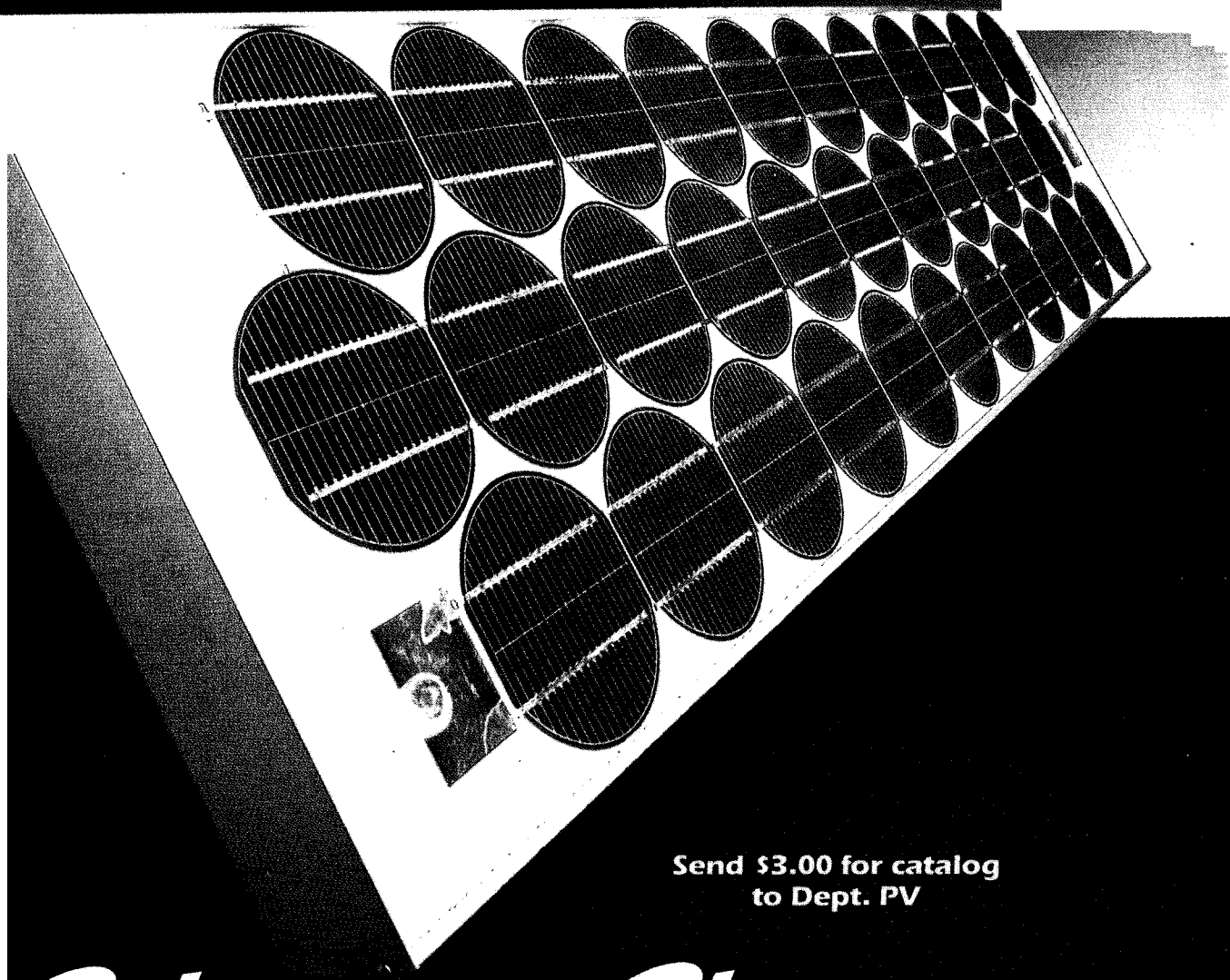

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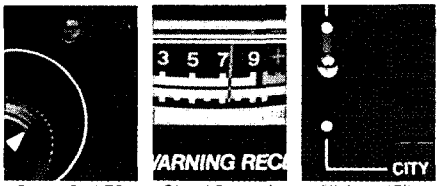

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